Foreign Agricultural Economic Report No. 65

P.L.480 Concessional Sales

- History
- Procedures
- Negotiating and Implementing Agreements

Economic Research Service U.S. DEPARTMENT OF AGRICULTURE

ABSTRACT

This report includes (1) the origin and history of Public Law 480, (2) general considerations in negotiating P.L. 480 agreements, (3) procedures for implementing the agreements, and (4) the real and monetary effects of P.L. 480 foreign currency transactions. The appendices of the report list P.L. 480 terminology and the uses made of foreign currencies accruing from transactions under the law. The report revises and expands "Financial Procedures Under Public Law 480," U.S. Dept. Agr. For. Agr. Econ. Rpt. 17, published in 1964.

Key Words: Public Law 480; concessional sales; balance of payments; foreign currencies.

Washington, D. C. 20250 September 1970

For sale by the Superintendent of Documents, U.S. Government Printing Office, Washington, D.C., 20402

PREFACE

This report revises and updates "Financial Procedures Under Public Law 480," Foreign Agr. Econ. Rpt. 17, published by USDA in 1964. Since that time, the Agricultural Trade Development and Assistance Act of 1954 (P.L. 480) has been amended; some of these revisions have effected changes in the financial and related procedures of the P.L. 480 program. Also, the accounting procedures used by the U.S. Treasury Department in its management of local currencies were streamlined and simplified after the previous report was published.

This report describes (1) the origin and history of P.L. 480, (2) the payment arrangements authorized for concessional sales, (3) general considerations in negotiating agreements between the United States and recipients of P.L. 480 commodities and (4) certain effects of local currency transactions. While most information has been included to inform readers unacquainted with the program, some information is not well known even to those experienced with P.L. 480. The program is quite extensive and new concepts have only recently been introduced into the administration of the act.

The information in this report was compiled to aid U.S. Government officials associated with the P.L. 480 program (especially those in the Departments of State, Treasury, Defense, Commerce, and Agriculture) and for officials of nations that receive aid through this program or that may expect to do so. It should also help private U.S. exporters who wish to enter the program, U.S. and foreign private entities that might receive loans of foreign currencies under conditions specified in the law, and U.S. and foreign banks engaging in international financial transactions. The report should also interest economists, farmers, educators, students, and all who are concerned with the simultaneous existence of overabundance and food shortages.

CONTENTS

P.L. 480 CONCESSIONAL SALES
• History • Procedures • Negotiating and Implementing Agreements

by

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BACKGROUND

Basic Objectives of Public Law 480

P.L. 480, 83rd Congress, as amended, states that it is U.S. policy "to expand international trade; to develop and expand export markets for U.S. agricultural commodities; to use the abundant agricultural productivity of the United States to combat hunger and malnutrition and to encourage economic development in the developing countries, with particular emphasis on assistance to those countries that are determined to improve their own agricultural production; and to promote in other ways the foreign policy of the United States."

Through the years some objectives of the act have changed. To fully appreciate the changes that have occurred, it is necessary to start many years before P.L. 480 became law.

Historical Setting of Enactment

The United States has had a farm problem since the short but deep business depression of 1920-21. After this depression, the prices of agricultural commodities did not recover as did prices in the nonagricultural sector. By the 1930's it was decided that both price supports and production controls were needed to solve the farm problem. The first national legislation dealing with both aspects was passed in 1933. Since then, it has been U.S. agricultural policy to (1) assure adequate supplies of farm commodities, (2) stabilize commodity markets and prices, and (3) equalize the farmer's bargaining position.

Certain basic approaches were used to achieve these goals. Price support programs were instituted which utilized loans, direct purchases, and direct payments to producers. Tied to price support programs were acreage allotments or marketing quota programs or some combination of the two. In addition, land retirement and adjustment or diversion programs were used in conjunction with price support programs, or as separate programs. Like acreage allotments and marketing quotas, these were instituted to bring production into reasonable balance with demand. Even with such programs, surpluses often occurred, and it became necessary to institute commodity storage, handling, disposal, and surplus removal programs.

From 1940 to 1953, requirements for agricultural commodities domestically and abroad were large enough to negate the problems of farm surpluses in this

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country. During World War II, the farm plant was asked to produce at maximum capacity. Immediately after the war, the world need for farm products, in a world torn by war, made significant demands on U.S. agriculture. By 1948 and 1949, however, the United States once again appeared to face the old "farm problem." The realized net income of farmers was $17.3 billion in 1947; it slipped in 1948, and by 1949 had dropped to $13.6 billion. While some farm surpluses accumulated in 1948 and 1949, the Korean conflict delayed a serious confrontation with the farm problem for several years. As this conflict grew more serious, many European nations rushed into the international market, buying and stockpiling against possible food shortages. By 1953, however, agricultural exports returned to more normal levels and in 1953 and 1954 stocks of farm commodities (including farm, commercial, and Government program holdings) increased significantly. Although acreage allotments and marketing quotas were reemployed, within the legal limits set in the 1930's, they proved inadequate in the face of steady increases in yields.

In 1954, agricultural surpluses were once again a recognized U.S. problem. This problem was compounded by the shortage of international purchasing power (dollars) in foreign nations needing U.S. farm commodities. This lack of dollars was not only a problem for the less developed countries (LDC's) but also for European countries, which in the mid-1950's were not earning many dollars. As a result, neither European countries nor the LDC's could import much from the United States, even though they needed U.S. agricultural products. A partial solution to this problem came with the passage of Senate Bill 2475, which on July 10, 1954, became Public Law 480. Under P.L. 480, a foreign nation could purchase U.S. farm products with its own nonconvertible currencies.

Amendments and Changes in Emphasis Since Enactment

Reflecting these problems, P.L. 480 in 1954 stated, among other things, that it was, "the policy of Congress, . . . to make maximum efficient use of surplus agricultural commodities in furtherance of the foreign policy of the United States . . . by providing a means whereby surplus agricultural commodities in excess of the usual marketings of such commodities may be sold through private trade channels . . ." Upon signing the law, the President of the United States issued a statement expressing his pleasure with legislation "designed to check the accumulation of surpluses." He also recommended ". . . that the burdensome stocks which had already accumulated be liquidated over a period of time . . ." Of major concern were the grain surpluses, particularly wheat.

Between 1954 and 1965, the policy expressed in P.L. 480 remained the same. Despite this policy, the 1961 ratio of carryover stocks of wheat to domestic use (including feed and seed) stood at 2.3 years. The corresponding ratio for 1954 had been only 1.5 years. Thus, the burdensome surpluses had not disappeared even though shipments under P.L. 480 and other Government programs had increased significantly.

The ratio of supply to use of wheat remained at 2.3 in 1962 but in the next 3 years it dropped sharply, and by 1965, it stood at 1.1 years. By mid-1966, the United States had less than a year's supply (0.8) on hand. At this point, the grain crop in India dropped drastically due to bad weather while

India's population was increasing by an estimated 12 million a year. Mass starvation was a possibility and the United States felt strongly obligated to assist India and other countries with similar problems, even though our carryover stocks were extremely low. This drastic change in circumstances demanded a change in policy. Amendments to P.L. 480 in that year deleted reference to U.S. surpluses and it became U.S. policy to use this country's abundant (but not unlimited) agricultural productivity to combat hunger and malnutrition. In addition, it became a part of U.S. policy to use its agricultural capacity to assist countries that were determined to improve their own agricultural production (the self-help program).

It has long been an objective of the United States to expand international trade through the use of various programs, including P.L. 480, particularly foreign trade in domestically produced agricultural commodities. In the days of surpluses, this was designed to reduce carryover stocks that stemmed from increased yields, despite acreage limitations. However, another problem arose in the late 1950's. In 1958 U.S. gold reserves declined by more than $2 billion and concern over our balance of payments increased. As a result, the need to use P.L. 480 as a means of improving our balance of payments position intensified. Through the years, amendments to the law were passed which increased the possible uses of local currencies generated by P.L. 480 agreements. Typically, these uses were tailored to reduce the necessity of obtaining local currencies with dollars in the process of executing official U.S. Government business. In 1959, dollar credit sales with long-term repayment periods were provided for in Title IV of the act and in 1962, provisions were added for U.S. and foreign private trade enterprise to enter into dollar credit (DC) sales agreements. In 1966, the provision for both types of DC sales was transferred to Title I and a new method called "convertible local currency credit" (CLCC) sales was added to this Title.

As concern over the U.S. balance of payments grew, the terms applied to DC sales stiffened. This concern also brought other changes. For example, since 1961 there has been a subsection which regulates the exchange rate used in P.L. 480 agreements. The language in this subsection was revised several times in an attempt to guarantee that the United States receive a realistic rate of exchange in countries with multiple exchange rates. A realistic exchange rate was vitally important to the United States in countries where U.S. requirements for local currencies were larger than the Government's supply. Also, an amendment to the act in 1966 required that the President take steps to assure a progressive transition from sales for foreign currencies to DC or CLCC sales. The transition is to be completed by the end of 1971.

Thus, 1966 represented a turning point in the history of P.L. 480. In addition to the policy changes incorporated into the law, the structure of the law was also revised considerably.

While some objectives of P.L. 480 have changed, certain goals have been present throughout. It has always been a stated objective of P.L. 480 to encourage economic development and to promote in other ways the foreign policy of the United States. Also, throughout the P.L. 480 program there has been the humanitarian aim of feeding hungry people around the world.

Brief Description of Present Act

There are four titles to the act, and in general the titles cover the following aspects:

Title I	Concessional sales
Title II	Donations and disaster relief
Title III	Barter
Title IV	General provisions and requirements

Title I is by far the most important in terms of commodities exported under P.L. 480. Just over 70 percent of all commodities shipped have been under this title. This includes (1) local currency (LC) sales, (2) long-term DC sales to foreign governments and private trade entities, and (3) CLCC sales. The various requirements and limitations placed upon the President in exercising the authorities given him in Title I are discussed more fully in subsequent sections of this report.

Under Title II, agricultural commodities can be donated to (1) meet famine or other ordinary relief requirements, (2) combat malnutrition, especially in children (3) promote economic and community development in friendly developing areas outside of the United States, and (4) for needy persons and nonprofit school lunch and preschool feeding programs outside the United States.

Title II states that commodities may be furnished through such friendly governments and such private or public agencies (including the United Nations World Food Program) as the President deems appropriate. Whenever practicable, however, nonprofit voluntary agencies which have been registered with, and approved by, the Advisory Committee on Voluntary Foreign Aid are used. All commodities furnished are clearly identified as a gift from the people of the United States. Under this title, the Commodity Credit Corporation (CCC) can pay for--in addition to the cost of acquisition--the packaging, enrichment, preservation, processing, transportation, and other incidental costs of the commodities supplied.

Title III provides for the barter or exchange of CCC owned agricultural commodities for (1) strategic or other materials which are not produced by the United States in sufficient quantities to meet U.S. needs, (2) materials, goods, or equipment required in connection with foreign economic and military aid and assistance programs, and (3) materials or equipment required in substantial quantities for off-shore construction programs. As much as is practicable, transactions under Title III are carried out through usual private trade channels. When engaging in such transactions, the U.S. Government must:

(1) take reasonable precautions to safeguard usual marketings;

(2) assure that Title III transactions do not unduly disrupt world prices of agricultural commodities or replace cash sales for dollars; and

(3) endeavor to preserve, in cooperation with other exporting countries, the normal patterns of

commercial trade for commodities covered by formal international marketing agreements to which the United States is a party.

The United States is permitted under the act to allow domestic processing of raw materials of foreign origin.

In recent years, most of the barter activities have been conducted under the authority of the CCC Charter Act rather than under the authority of P.L. 480. The Charter Act includes, among other things, provisions for the removal and disposition of surplus agricultural commodities. It also provides for the exportation of, and development of foreign markets for, agricultural commodities. The commodities involved in these transactions have come mostly from privately owned stocks. The emphasis has been on exports of agricultural commodities in connection with various types of offshore procurement of materials and services needed by the Department of Defense, the Agency for International Development, and other agencies which reimburse CCC.

Title IV covers a number of general aspects of P.L. 480. For example, it states that the programs of assistance undertaken pursuant to P.L. 480 are intended to serve both humanitarian objectives and the national interest of the United States. Such assistance shall be used in a manner to assist friendly nations that are determined to help themselves toward a greater degree of self-sufficiency in food production and in resolving their problems relative to population growth. Title IV further states that no agricultural commodity can be made available for export under P.L. 480 if the disposition would reduce the U.S. supply of that commodity below that needed to meet (1) domestic needs, (2) adequate carryover, and (3) anticipated commercial export requirements. Title IV defines "agricultural commodities" as used in the act to include any agricultural commodity produced in the United States or product manufactured in the United States from an agricultural commodity. However, this does not include alcoholic beverages, and for the purposes of Title II, tobacco or tobacco products. For the purpose of P.L. 480, domestically produced fishery products are also defined as "agricultural commodities."

Under Title IV the United States has authorized a farmer-to-farmer assistance program to help farmers in the recipient country increase the effectiveness of their farming and marketing operations. Further provisions enable farm youth and farm leaders from the recipient country to be brought to the United States for training and enables the United States to conduct research for the purpose of improving the production and distribution of tropical and subtropical agricultural products. As much as $33 million per fiscal year can be appropriated for these activities. However, these provisions have not yet been implemented.

The act, as amended on December 31, 1966, established under Title IV an advisory committee to survey general policies relating to the administration of P.L. 480. The committee surveys (1) the manner of implementing self-help provisions, (2) the use of foreign currencies accruing from foreign currency agreements, (3) the currencies reserved for loans to private industry, (4) the exchange and interest rates used, and (5) the terms applied to credit sales. Members of the advisory committee include the Secretaries of State, Treasury, and Agriculture, the Director of the Bureau of the Budget, the Administrator of the Agency for International Development, the chairman and the ranking minority member of the House committees on (1) Agriculture and on (2) Foreign Affairs, and the chairman and the ranking minority member of the Senate committees on (1) Agriculture and Forestry and on (2) Foreign Relations.

The President is required by Title IV to report to Congress by April 1 each year on the activities performed under P.L. 480 during the preceding calendar year. This report is available to the public.

Magnitude and Success of the Act

There is no way of accurately estimating the number of people who have consumed P.L. 480 food. At some time, nearly every country in the world has received P.L. 480 food under one type of program or another. Total exports under P.L. 480--from the inception of the law in July, 1954 through June, 1969--had an export market value of $18.2 billion (table 1). Of this amount, sales for local currencies accounted for $11.6 billion (64 percent); credit sales, $1.4 billion (7 percent); grants (donations) $3.5 billion (19 percent); and barter for strategic materials, $1.7 billion (10 percent). The peak year for shipments under P.L. 480 was FY 1965 when $1.6 billion was exported.

Exports under local currency agreements reached a peak of over $1.1 billion in FY 1965, and have since declined to $337 million in FY 1969 (fig. 1). This decline is largely a result of the requirement in the 1966 extension of P.L. 480 that local currency sales be ended no later than December 31, 1971. Part of the decline may also reflect the overall decline in shipments under P.L. 480 that has occurred since FY 1965.

While local currency sales have declined since FY 1965, exports under credit sales agreements (the first of which were made in FY 1962) have risen steadily. They increased from $19 million in FY 1962, to $158 million in FY 1965, and to $411 million in FY 1969. As stated earlier, the original credit program was for DC sales only. Beginning January 1, 1967 CLCC sales were added as a type of credit for countries that could not go directly from local currency sales to dollar credit sales.

Donations increased from $187 million in FY 1955 to $265 million in FY 1969. Since FY 1961, they have fluctuated between $240 million and $270 million a year. The barter program under P.L. 480 in the late 1960's was extremely small, but it was fairly significant in the late 1950's. However the data on these shipments are not historically comparable because, prior to 1963, the data include some shipments made under authorizations other than P.L. 480.

During 1954-69, the countries receiving the greatest value of goods under P.L. 480 were: India, $4.3 billion; Pakistan, $1.3 billion; Yugoslavia, $1.0 billion; the United Arab Republic, $911.7 million (however, sales agreements with the U.A.R. have been prohibited since 1966); the Republic of Korea, $941.4 million; Brazil, $780.5 million; and Spain, $617.8 million2/. Several countries

2/ See: 1969 Annual Report on Public Law 480, Food For Peace.

Table 1.--Exports under P.L. 480 by type of agreement, value and percentage of total, fiscal years 1955-69

Fiscal year	Total	Sales for local currency	Long-term dollar and convertible local currency credit sales	Government-to-government donations for disaster relief and economic development	Donations through voluntary relief agencies	Barter 1/
	Million dollars 2/					
1955	385	73	--	52	135	125
1956	984	439	--	63	184	298
1957	1,525	908	--	51	165	401
1958	982	658	--	51	173	100
1959	1,017	724	--	30	131	132
1960	1,116	824	--	38	105	149
1961	1,317	951	--	75	147	144
1962	1,496	1,030	19	88	161	198
1963	1,452	1,088	58	89	170	47
1964	1,415	1,056	46	81	189	43
1965	1,572	1,142	158	57	183	32
1966	1,346	866	181	87	180	32
1967	1,270	803	178	110	157	22
1968	1,287	723	306	100	152	6
1969	1,014	337	411	111	154	1
1955-69 cum.	18,178	11,622	1,357	1,083	2,386	1,730
	Percent					
1955	100	19	--	14	35	32
1956	100	45	--	6	19	30
1957	100	60	--	3	11	26
1958	100	67	--	5	18	10
1959	100	71	--	3	13	13
1960	100	74	--	3	9	13
1961	100	72	--	6	11	11
1962	100	69	1	6	11	13
1963	100	75	4	6	12	3
1964	100	75	3	6	13	3
1965	100	73	10	4	12	2
1966	100	64	13	7	13	2
1967	100	63	14	9	12	1
1968	100	56	24	8	12	3/
1969	100	33	41	11	15	3/
1955-69 cum.	100	64	7	6	13	10

1/ Before 1963 includes some shipments under authorizations other than P.L. 480.
2/ Export market value.
3/ Less than ½ percent.

VALUE OF U.S. AGRICULTURAL EXPORTS UNDER P.L. 480

By Type of Sale

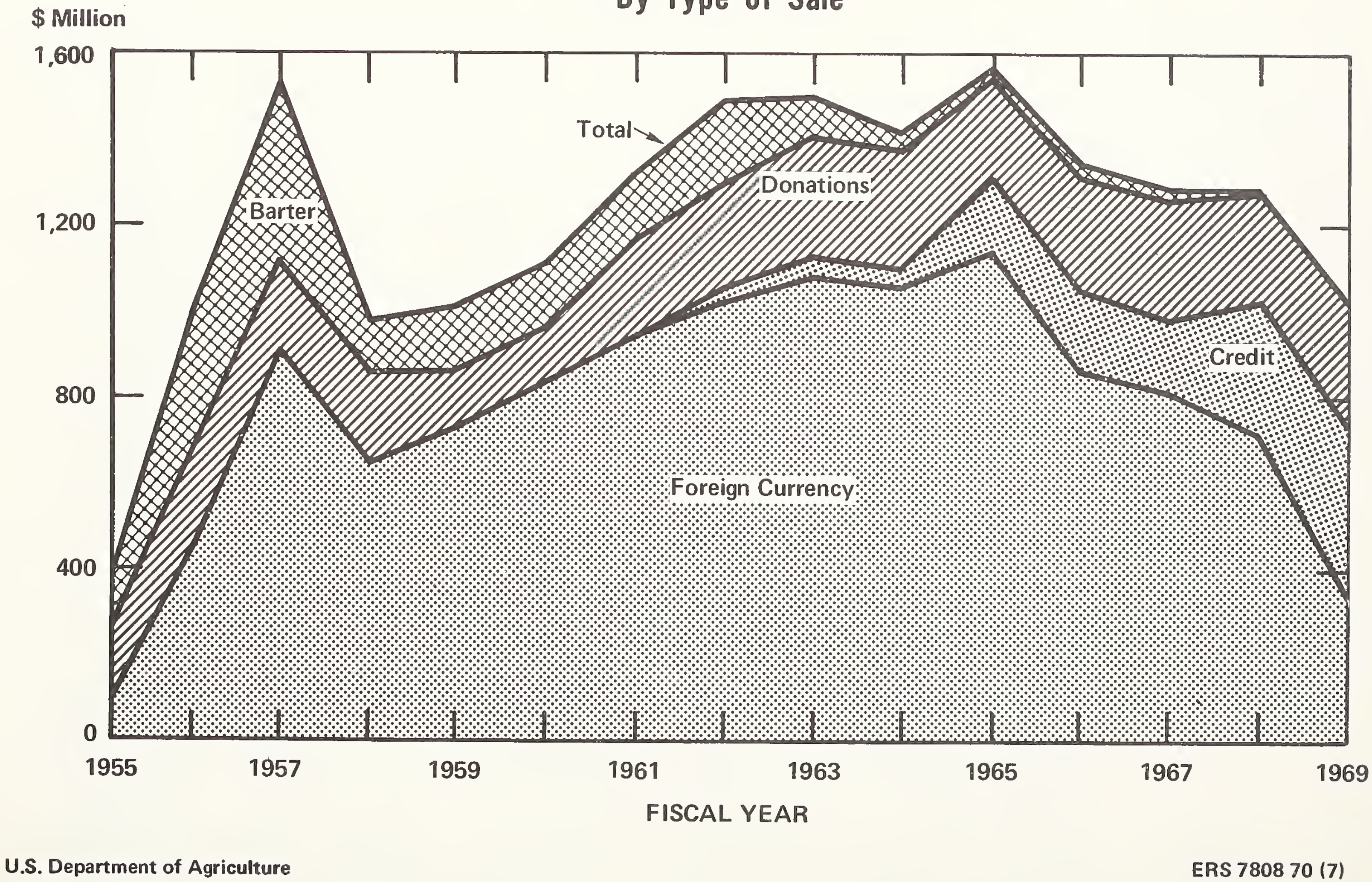


Figure 1

that formerly imported food under P.L. 480 have progressed economically and financially to the point where such imports are no longer necessary. Many factors were responsible for their progress, but there is general agreement that P.L. 480 contributed to their development. Equally important is the role that P.L. 480 has played in the development of countries still receiving P.L. 480 commodities.3/

Grains and grain products (especially wheat, flour, and rice), cotton, vegetable oils, nonfat dry milk, and tobacco have composed the bulk of P.L. 480 exports over the life of the program. Shipments of meat, poultry, fruits and vegetables, and oilseeds and meal have been relatively minor because these products are not normally included in the program. They are either in short supply relative to demand in the United States, or are not requested by recipient countries because of higher unit costs resulting from the storage, processing, and transportation required.

From July 1954 through December 1969, shipments of major products included 4.8 billion bushels of wheat worth $8.0 billion; 15.9 million bales of cotton worth $2.1 billion; $1.5 billion of dairy products; 11.0 billion pounds of vegetable oils valued at over $1.4 billion; 31.1 billion pounds of wheat flour worth in excess of $1.2 billion; over 19.1 billion pounds of rice worth more than $1.2 billion; and 759 million pounds of tobacco worth $544 million.

Local currency sales accounted for more than 70 percent of the wheat, vegetable oils, cotton, and tobacco shipped under the P.L. 480 program. Credit sales accounted for not more than 20 percent of the value of any of the major P.L. 480 products mentioned above.

Donations accounted for the majority of P.L. 480 shipments of wheat flour (57 percent) and dairy products (87 percent). Donations also accounted for 22 percent of vegetable oils exported under the program.

Barter agreements accounted for 23 percent of the tobacco shipments and about 15 percent of cotton exports under P.L. 480. Barter was of little importance to wheat flour, vegetable oil, and dairy shipments, and accounted for less than 8 percent of P.L. 480 wheat exports. However, roughly one third of all feed grain shipments under P.L. 480 were made as a result of barter transactions.

P.L. 480 shipments have made a positive contribution to the U.S. balance of payments. From the beginning of the program through December 1969, the balance of payments benefits from P.L. 480 shipments amounted to $2.6 billion. These benefits in FY 1969 alone amounted to $296 million. The means whereby P.L. 480 contributes to the U.S. position is discussed below under "Financial Arrangements" and "Real and Monetary Effects of Local Currency Transactions".

3/ See: Barlow, Frank D., Jr. and Susan A. Libbin. Food Aid and Agricultural Development, U.S. Dept. Agr., For. Agr. Econ. Rpt. 51, June 1969. This publication contains an extensive bibliography.

Mechanics of Negotiating an Agreement

A Title I P.L. 480 government-to-government agreement is usually initiated by a request from a foreign government to the U.S. Embassy in that country. Private trade credit sales agreements, however, are usually negotiated in Washington, D.C. with the private entity. The subsequent discussion in this section deals with government-to-government agreements.

The foreign government's request, with U.S. Embassy recommendations, is forwarded to Washington and all appropriate U.S. agencies are notified. In response to the request, USDA has the responsibility of developing P.L. 480 proposals for interagency consideration. Position meetings within the Department are organized and conducted by a program coordinator in the Export Marketing Service. In these meetings all the factors involved in the P.L. 480 program are considered. The proposal developed by USDA is presented to the Interagency Staff Committee on P.L. 480 (ISC), which USDA chairs. Other members of the ISC are State-AID, Treasury, Commerce, Defense, and Bureau of the Budget. Prior to developing a proposal and presenting it to ISC, USDA often confers with other members of the ISC to help avoid potential problems and to expedite the development of a program.

ISC members have areas of primary responsibility in addition to the overall program. For example, USDA is responsible for financing sales of agricultural commodities to foreign markets and is concerned with the effects of P.L. 480 shipments on commercial markets. AID is concerned with the foreign country's political, economic, and social development. State (Bureau of Economic Affairs) is concerned with the economic and political foreign policy implications of P.L. 480. It consults with countries that have an established trade interest in the commodities included in the proposed agreements to assure them that such programs will not unduly interfere with normal commercial trade. All agencies--but especially the Bureau of the Budget and the Treasury Department--are concerned with the financial ramifications of a program.

The Committee thoroughly considers such factors as (1) legislative requirements and objectives, (2) future U.S. needs for local currency in the recipient country, (3) import requirements of that country in relation to domestic production, (4) usual marketings of the United States and effects on traditional suppliers, (5) the possibilities for barter or other U.S. trade programs and (6) the effect of the program upon the U.S. balance of payments and budget. The recipient country's internal and external financial position is analyzed to determine whether the country should purchase on a commercial or concessional basis and, if the latter, whether for local currencies, long-term dollar credit, or convertible local currency credit, or some combination thereof.

The proposal is analyzed, modified, and accepted or rejected by the ISC. If an agreement includes either a DC or CLCC sale, or both, it is submitted to the National Advisory Council on International Monetary and Financial Policies (NAC) and its views are requested.

Following ISC clearance, and review by NAC when necessary, negotiating instructions are prepared. These are cleared with all interested U.S. Government agencies, and transmitted by the Department of State to the appropriate U.S. Embassy. The ambassador or his designees, such as the agricultural attache and AID officials, meet with officials of the host government and negotiate the terms of a sales agreement. The U.S. officials contact Washington for clarification and supplementary instructions when necessary. Any changes in an agreement which develop during negotiations must be authorized by Washington. When agreement between the United States and the foreign country has been reached, the U.S. Embassy must give 72 hours advance notice to Washington (not including weekends and holidays) before the agreement can be signed. As soon as notice is received, Congress is notified, and a public notice is prepared for release when the agreement is signed.

GENERAL CONSIDERATIONS IN NEGOTIATING AGREEMENTS

Many economic, financial, commercial, and foreign policy factors must be considered before a concessional sales agreement can be signed between the United States and a foreign nation or a private trade entity. Consideration is required by law for some of these factors; it is required by national policy or administrative regulations for others. It usually takes weeks to collect and analyze all the pertinent information and to reach agreement on all points. However emergencies sometimes require that P.L. 480 government-to-government agreements be fashioned so they can be developed promptly for formal signing. On the other hand, circumstances may be so complex that it takes months to reach agreement, and in a few cases no agreement is ever reached.

This section presents in nontechnical terms the major factors which require consideration. These factors have been grouped under three major classifications--(1) financial arrangements, (2) commercial factors, and (3) foreign policy considerations. Of course, most factors do not fit exclusively into one classification so they are placed in the group in which they seem to fit best.

Financial Arrangements

The economic and financial factors that must be considered are best brought to light in a discussion of the various payment arrangements that have been devised over the years to meet different economic conditions. As already stated, the objective of concessional sales is to provide a method whereby countries with foreign exchange shortages can purchase U.S. agricultural commodities. After the P.L. 480 program had operated for a number of years, the program also gradually became a means of improving the U.S. balance of payments position. However these two objectives tend to conflict. To balance these objectives, two basic payment methods have been instituted: (1) immediate payment in currencies of the recipient country (local currency sales) and (2) two forms of credit, (a) dollar credit, and (b) convertible local currency credit. After 1966, many sales agreements (except for those with private trade entities) have been a combination of these methods, the mixture depending to a large extent upon the recipient country's external financial position. These arrangements apply to the purchase of commodities--the financial procedures with regard to covering the cost of ocean transportation are covered below, as are several other financial considerations that are now incorporated into the law.

Local currency sales.--P.L. 480 as passed in 1954 provided only for local currency sales. Under this arrangement the United States receives, as payment, the currencies of the recipient country and reaches an agreement with that country on their use.

Normally, these currencies can only be spent in the recipient country and are not accepted as a medium of exchange in international transactions. This being so, these currencies do not help the United States improve its balance of payments except when they are used to meet U.S. obligations in the recipient country which would have been met with dollars. Therefore,the law now requires that limited amounts of local currencies be convertible to dollars. However, care must be taken to avoid requiring a conversion so large as to place a burden on the limited foreign exchange reserves of most recipient countries and thus be inconsistent with the assistance aspects of the act. Consequently, data on the present external financial position of the recipient country must be gathered and analyzed and the country's position in the near future assessed to the extent possible. With this information, a decision can be made as to the percentage of local currencies that should be converted to dollars.

Regardless of the country's position, the law requires that not less than 2 percent of the currencies be convertible into other currencies to be used in any foreign country to help develop new markets for U.S. agricultural commodities. Furthermore, in countries where the U.S. Government has more local currency than it needs in the next 2 years (that is, in excess-currency countries), the agreement must provide for convertibility of currencies equivalent to the normal expenditures of American tourists in the country. However, such amount need not exceed 25 percent of the currencies received under the agreement. Sales to American tourists, convertibility for market development, and convertibility for other purposes all count against this requirement.

The law also requires that not less than 5 percent of the total local currencies that become available to the United States in any year shall be set aside for market development. As a matter of policy, the U.S. Government sets aside not less than 5 percent of each agreement. The 2 percent that must be convertible for market development (discussed in the prior paragraph) counts as part of the 5 percent that must be set aside. However, the Secretary of Agriculture may release certain currencies if he determines they can not be effectively used for market development.

Furthermore, 2 percent of the sales proceeds received each year in each country must be made available to finance international education and cultural exchange programs. In nonexcess-currency countries, not less than 20 percent of the aggregate amount of local currencies that accrue from LC sales and loan repayments can be used only as provided for annually in appropriation acts. However, the President is authorized to waive this requirement.

The bulk of the local currencies the United States receives as payment are used in the recipient country, but the particular use to be made of these currencies becomes a matter of negotiation. The procedures and factors that must be considered are very involved and are discussed in detail below (see, "Local Currency Transactions" and "Real and Monetary Effects of Local Currency

Transactions"). In short, currencies may be used to benefit the United States, or the recipient country, or sometimes both.

Dollar credit sales, government to government.--In 1959, a provision was added to P.L. 480 whereby sales could be made on credit, with payment of principal and interest in dollars. There are now two kinds of dollar credit sales agreements, government-to-government and private trade credit sales; each type of agreement has its own set of terms and conditions. Government-to-government trade agreements have been permissible since dollar credit sales were authorized in 1959. Private trade credit sales were authorized by amendments to the act in 1962. The authorization for dollar credit sales of both kinds was under Title IV of the act and for a number of years these sales were commonly referred to as "Title IV" sales. Local currency sales were referred to as "Title I" sales. However, in the 1966 amendments to the act, all concessional sales arrangements were placed under Title I, and it is no longer appropriate to use the terms "Title I" and "Title IV" sales.

Government-to-government agreements have been by far the most common. The maximum credit period allowed under the arrangement is 20 years. The United States is permitted to allow the recipient government to go a maximum of 2 years before making the first principal installment. The entire 2 year period is often called a grace period. The rate of interest during this period is often lower than the rate charged subsequently. Within these limits the length of the total credit period and the grace period are negotiable considerations. These periods customarily begin on the date of last delivery in any calendar year. Thus if commodities are delivered in two calendar years under one agreement, two repayment schedules are necessary.

Payments of principal are to be made in reasonable annual amounts, and in practice they are usually repaid in equal annual installments. Interest is calculated on the unpaid balance. The minimum interest rates are not less than the minimum rates required by the Foreign Assistance Act of 1961, as amended; currently, this is 2 percent during the grace period (the "initial" interest rate) and 3 percent thereafter (the "continuing" interest rate). Interest is computed from the date of last delivery in each calendar year. Within these limits, the terms are as favorable to the United States as the economy of the recipient country will permit.

Private trade credit sales agreements.--Agreements between the U.S. Government and private trade entities (PTE's) are commonly referred to as private trade agreements (PTA's). Any private trade entity of the United States or of a foreign country friendly to the United States may participate in this program. The PTE must be engaged in private enterprise or other nongovernmental activity. It may be an individual, partnership, corporation, cooperative, or association.

The PTE obtains commodities from the open market and CCC provides a line of credit through a commerical bank. The PTE uses this to pay the U.S. supplier of the commodities and for ocean transportation. At the same time, it incurs a debt obligation in dollars with the CCC. The maximum grace period is 2 years and the maximum credit period is 20 years. Whenever practicable, the PTE is required to pay 5 percent of the purchase price of the commodity on delivery.

Although the repayment period of agreements signed thus far has ranged from 2 years to 19 years, most range from 6 to 15 years. As with government-to-government programs, the credit and grace periods begin on the date of last delivery in any calendar year. The interest rate charged on private trade agreements is equivalent, as nearly as practicable, to the average cost of funds to the Treasury on outstanding marketable U.S. securities having maturities comparable to the maturity of the credits extended in the PTE agreement. However, in no event is the rate less than the minimum rate specified for government-to-government dollar credit agreements. The principal and interest due on these credits are paid in dollars. Payments must be guaranteed by assurers (guarantors) acceptable to CCC. The guarantee of payment is in the form of an irrevocable commitment issued by an acceptable financial institution in the United States or in a foreign country. This includes, but is not limited to, central banks or governmental financial agencies or the governments of friendly foreign nations.

When the PTE sells the commodities in the specified country he of course receives payment in local currencies. The proceeds from the sale must be used to develop and execute projects in the recipient country as specified in the agreement. These projects must result in the establishment of facilities designed to improve the storage or marketing of agricultural commodities, or which will otherwise stimulate and expand private economic enterprise. The repayment of the dollar obligation by the PTE is based upon the cash flow of local currencies which the development project will be reasonably expected to generate.

PTE loan agreements should not be confused with "Loans to Private Enterprise," commonly called "Cooley loans." (Former Congressman Harold Cooley introduced the amendment to P.L. 480 which authorized such loans.) Cooley loans are made to private businesses abroad for similar purposes, but they are loans of local currency from the proceeds accruing to the United States under Title I government-to-government local currency sales agreements. Cooley loans may be, and usually are, repaid to the U.S. Government in the local currency lent. PTE loans must be paid in dollars.

<u>Convertible local currency credit sales</u>.--In the 1966 amendments to the law, Congress directed that a transition be made from local currency sales to dollar credit sales by the end of 1971. It specified that to the extent a transition to dollar credit sales was not possible, a transition could be made to credit sales for foreign currencies which could be converted into dollars. Thus came into being the fourth type of agreement, convertible local currency credit (CLCC) sales. From the viewpoint of both the United States and the recipient country, these may be considered payable in dollars, since the option for convertibility lies with the United States. In this respect, CLCC loans do not differ from DC loans. All CLCC agreements are on a government-to-government basis.

The law specifies that CLCC sales be made on credit terms no less favorable to the United States than those for development loans made under the Foreign Assistance Act of 1961, as amended. Currently, loans made under this act are for a maximum credit period of 40 years, with a grace period not to exceed 10 years. As with DC sales a minimum interest rate of 2 percent applies during the grace period and a rate of 3 percent during the remainder of the credit period. Unlike DC sales, interest charges start from the date on which delivery is made. Depending on the external financial position of the recipient country, the terms in any agreement may be stiffer than the terms of maximum leniency.

In government-to-government DC or CLCC agreements, the foreign government acquires local currency through the resale of the commodity within the country. The local currency value is usually equivalent to the dollar value of the commodities acquired under the agreement. The law specifies that each agreement provide that these currencies are used for economic development purposes that are mutually agreed upon by the two governments.

Ocean transportation.--The Cargo Preference Act (Public Law 664, 83d Congress, which amended the Merchant Marine Act of 1936) requires that at least 50 percent of the quantity of all products exported under certain U.S. Government programs be shipped on U.S.-flag vessels to the extent that these vessels are available at fair and reasonable rates for commercial U.S. flag vessels. This requirement applies, among other things, to concessional sales and donations under P.L. 480. Sales of fresh fruit and fruit products under Title I of P.L. 480 are exempt from this requirement as are shipments between foreign countries of commodities and defense articles purchased with foreign currencies generated by P.L. 480.

Most freight rates on U.S.-flag vessels on some trade routes are higher than rates charged by other vessels on the same route. CCC reimburses the importer for all the amount by which the freight bill for the portion required to be carried in U.S.-flag vessels exceeds the dollar equivalent of the freight bill for an equal quantity carried in foreign-flag vessels (fig. 2). This excess is commonly referred to as the "ocean freight differential." The existence and magnitude of this differential is subject to determination by CCC. If a trade route is served by companies which are members of a steamship conference, there is generally no differential since rates most often are identical.

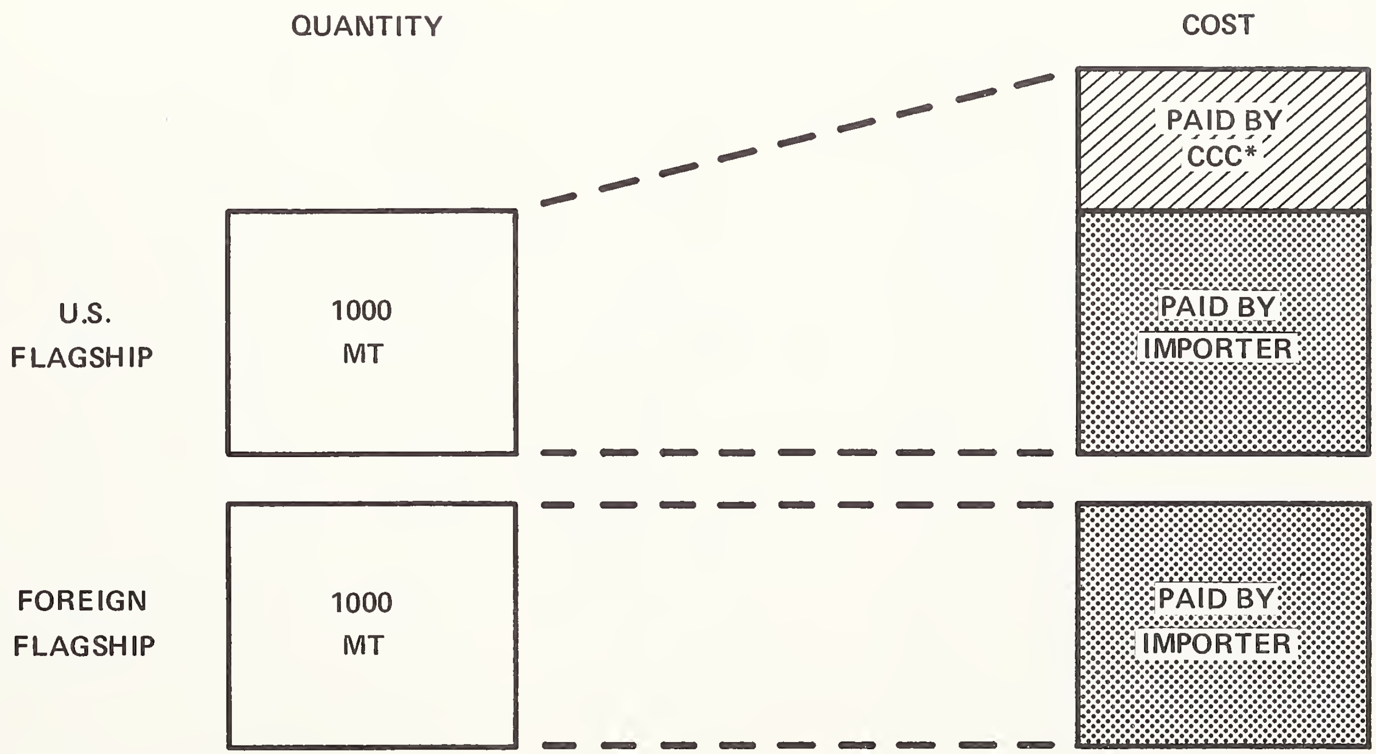
Except for the differential, the cost of transporting commodities must be paid by the importer. The importer--either a private firm, or in some countries, a government agency--pays this amount in cash or otherwise finances it on his own initiative.

Freight bills are usually payable in dollars or other hard currency and thus constitute a drain on the foreign exchange reserves of the recipient country. To partially alleviate this drain, the U.S. Government, prior to FY 1970 (July 1, 1969), sometimes extended credit to the recipient government (not the importer) to offset the dollar cost of the portion carried in U.S.-flag vessels.4/ This credit was extended only when the commodities involved were sold under a credit sales agreement, either DC or CLCC. The amount of the credit was equal to the freight bill on the quantity carried on U.S.-flag ships, minus the ocean freight differential--in other words, the cost of

4/ Credit may also be extended to private trade entities under private trade agreements. This type of credit was not stopped on July 1, 1969.

OCEAN TRANSPORTATION

ILLUSTRATIVE COST AND PAYING ENTITY



* OCEAN FREIGHT DIFFERENTIAL. EXISTENCE AND MAGNITUDE SUBJECT TO DETERMINATION BY CCC.

U.S. Department of Agriculture ERS 7805 70 (7)

Figure 2

transporting the quantity actually carried on U.S.-flag ships, but based on foreign-flag freight rates. The credit, when extended, was incorporated with the loan on the commodities and the same credit terms applied.

The decision to cease financing the dollar cost described above was made because of U.S. budgetary limitations. If budget conditions improve, this decision may be revised.

Initial payment.--P.L. 480 requires that, whenever practicable, not less than 5 percent of the purchase price of commodities sold under P.L. 480 be payable in dollars or other convertible currencies upon delivery of the commodities. This payment is called an "initial" payment, or in some cases, a "cash" payment. This requirement represents a hardening of P.L. 480 terms and was instituted to aid the U.S. balance of payments.

On most credit agreements signed since the beginning of 1967, it has been practicable to include an initial payment. However, the initial payment has sometimes been less than and sometimes greater than 5 percent. Countries which qualify financially for LC agreements are less able to make an initial payment than countries receiving DC or CLCC agreements. Consequently, the initial payment required of these countries has normally been reduced by the amount of the convertibility requirement. As stated above, under "Local Currency Sales," a certain percentage of the local currencies generated in each LC agreement must be convertible into dollars or, at the option of the United States, other designated foreign currencies. Since the convertibility requirement and initial payments both aid the U.S. balance of payments, the amount of the initial payment may be reduced by the amount of the convertibility requirement. In some cases, this accounts for the initial payments being less than 5 percent in LC agreements. Whatever the percentage term may be, it is applied to the commodity value--not to the total value of the agreement, which may also include transportation cost.

In practice, an initial payment is effected in the following manner: CCC finances, through the letter of commitment, a value which is less than the value of the commodity purchased under the sales agreement. The difference between these two values is equal to the initial payment. Since the difference is not financed by CCC, the importer must arrange for payment of this amount to the exporter in the United States not later than delivery f.o.b. vessel.

Currency use payments.--As the shift from LC sales to credit sales progressed in 1967 and 1968, the United States no longer acquired enough local currencies in some countries to meet its current obligations. Under DC agreements, the United States does not acquire local currencies. Under CLCC agreements, the repayment in local currencies is optional, but in any case is not immediate because of the long grace period normally extended. During the grace period (up to 10 years), the United States receives only interest payments and these, typically, are small. Thus, if local currencies were needed by the United States but were not available from P.L. 480 or other local currency accounts, they were purchased from commercial sources with dollars. This adversely affected the U.S. balance of payments. In the 1968 amendments to P.L. 480, Congress added the proviso that, except where the President determined that it would be inconsistent with the objectives of the act, he shall determine the amount of local currencies needed for uses specified in subsections (a), (b), (c), (e), and (h) of section 104 (see appendix B). The agreement shall provide for payment of such amounts in dollars or foreign currencies upon delivery of the agricultural commodities. A local currency payment under this arrangement has come to be known as a "currency use payment" (CUP) and credit sales agreements now provide for such payment. The implementation of the CUP is discussed below.

While the CUP is helpful, it seldom is large enough to cover U.S. local currency needs. In many countries, U.S. needs are as large or larger than the entire value of the P.L. 480 program. To require a 100-percent CUP from these countries would in effect constitute a commercial rather than a concessional sale and is therefore not requested.

According to the act, the CUP is to be made when the commodities in the agreement "are delivered." In practice, the payments are required to be made upon demand by the United States during the period of delivery under the agreement.

A CUP may be considered as an advance payment of the earliest installments of principal and interest. These installments, payable in dollars, may be forgone until their value equals that of the CUP. Interest is calculated so that the recipient country does not pay interest on the portion of the credit represented by the CUP, since the United States has the immediate use of the funds included in these payments. The amount of local currencies to be paid as a CUP are stated as a percentage of the total value of the agreements and not as an actual dollar value. The percentage rate is applied to the amount of credit extended; that is, the commodity value plus any credit extended to cover transportation costs, minus any initial payment made.

Currency use payments are not normally needed and therefore not included in agreements with countries where the United States owns more foreign currencies than will be needed in the next 2 years.

Exchange rates.--In P.L. 480 agreements with countries that maintain multiple exchange rates, the problem of which rate to use in P.L. 480 transactions has been a thorny one. To obtain the highest rate to be used in depositing local currencies to the account of the United States, or in converting local currencies to dollars or third-country currencies, Congress has consistently tightened the exchange rate provision of the act. The current legislation specifies that the President shall "obtain rates of exchange applicable to the sale of commodities under such agreements which are not less favorable than the highest of exchange rates legally obtainable in the respective countries and which are not less favorable than the highest of exchange rates obtainable by any other nation" (section 103 h).5/ No such problem arises in countries that maintain a unitary exchange rate.

Other financial considerations.--Two amendments contained in the 1968 legislation authorize convertibility of up to 50 percent of the foreign

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5/ For a more detailed discussion of P.L. 480 exchange rates, see Rice, Gabrielle P. "P.L. 480 Legislation and Multiple Currency Practices", Foreign Gold and Exchange Reserves, U.S. Dept. Agr., FGER-3, May 1967.

currencies received pursuant to LC agreements. One amendment stipulates that currencies may be sold to U.S. contractors or contractors in the purchasing country for the payment of wages earned by their employees in the development of public works in the purchasing country (section 103 p). The other amendment authorizes the sale of currencies to U.S. importers to purchase commodities or materials in the purchasing country (section 103 q). These two amendments are intended to assist in improving the U.S. balance of payments position without impairing the objectives of P.L. 480.

Commercial Factors

Since the concept of concessional sales was first introduced many people have been concerned that such sales would displace commercial exports, not only those of the United States, but also those of friendly foreign nations. Such is not the intention of the United States. In accordance with this policy, P.L. 480 requires that reasonable precautions (maximum precautions in the case of dollar credit sales) be taken to safeguard the usual commercial markets of the United States and to assure that concessional sales will not unduly disrupt world prices of agricultural commodities or normal patterns of commercial trade with friendly countries.

Usual marketing requirements (UMR's).--In conformity with the law, recipient countries must continue importing from their normal commercial sources the same kind of commodities that are included in an agreement. The specified quantity required to be purchased is normally based on the quantity actually imported commercially in recent years, but this can be modified according to the country's ability to import. Only imports from friendly countries are considered in establishing UMR's. The UMR is stated on a total basis; that is, imports from particular countries are not stated in the agreement except that in some agreements a UMR for commodity purchases from the United States is given.

Transshipment.--Another requirement in the law which helps to maintain normal patterns of commercial trade is that commodities will not be imported by the recipient country on a concessional basis and subsequently exported without specific U.S. approval. Since the recipient country purchased the commodities on less than a commercial basis it would be possible for it to undersell the world price and, thereby, disrupt the world market. Transshipment would also be contrary to the principle of a "need for the commodity" in the recipient country, which is an underlying principle of P.L. 480.

Exporting similar commodities.--To protect normal commercial patterns, the prohibition on transshipments is reinforced with limitations on the export of commodities considered to be the same as, or like, the commodities included in a particular agreement. Without such a requirement, a nation might import one commodity under P.L. 480 and substitute for it on the world market a commodity which it produces domestically and has traditionally consumed. A country might also import a P.L. 480 commodity, process it into a more finished commodity, and then export that product at less than world market prices. Since the imported commodity was obtained under a concessional sale, it becomes a relatively cheap raw material or input for the more finished commodity. For these reasons the concept of "same as, or like," has been defined broadly. For example, corn is classified as being the same as, or like, grain sorghum (except in Latin America); textiles made from cotton the same as, or like, cotton; and pasta products the same as, or like, wheat or wheat flour. Each P.L. 480 agreement specifically defines the same-or-like commodities.

Export limitations assure that the commodities supplied by the United States under the agreement are needed and that the ultimate point of consumption is the country entering into the P.L. 480 agreement. The intent is not to supply commodities, or similar or like commodities, for sale in world commercial markets, either in processed or unprocessed form.

Each agreement also specifies an export limitation period, during which the same-or-like commodities cannot be exported by the recipient country without specific U.S. approval. The period is usually specified as beginning when the agreement is signed and ending when the last commodities under a particular agreement are imported and utilized, or by reference to a particular calendar or fiscal year.

Third-country consultations.--In assuring that commercial patterns and world prices will not be disrupted, the U.S. Government consults with friendly foreign nations that historically are either large exporters of the commodities involved or exporters of such commodities to the particular nation requesting a P.L. 480 agreement. These consultations are held to determine what effect, if any, future shipments might have. Many consultations are necessary since the United States exports such a wide variety of commodities under P.L. 480.

Fair share.--The law requires that the President shall "take steps to assure that the United States obtains a fair share of any increase in commercial purchases of agricultural commodities" by P.L. 480 recipients.

Foreign Policy Considerations

A number of foreign policy provisions and restrictions must be included in a P.L. 480 agreement or, at least, considered before an agreement is signed. These provisions and restrictions may be required by P.L. 480 itself or by other laws which apply to P.L. 480 transactions, particularly the various foreign assistance acts. These requirements are mentioned here for the reader's information; the law should be reviewed for a definitive statement on each provision or restriction. Many of the restrictions were not a part of the law when it was first passed but were included as conditions changed.

Assistance to friendly countries.--The President is to use the act to assist friendly countries to be independent of domination or control by any world Communist movement.

Unfriendly or aggressive nations.--The President may not enter into Title I agreements with countries unfriendly to the United States. This generally includes countries controlled or dominated by a foreign government controlling a world communist movement plus, for foreign currency sales, any countries dominated by a communist government. It also includes countries that sell or furnish or permit their ships or aircraft to transport equipment, material or commodities to North Vietnam and Cuba--with certain exceptions in the case of Cuba. Title I sales to the United Arab Republic are prohibited unless the President determines that it is in the national interest.

P.L. 480 further provides that no sales under the act shall be made to any country which is (1) an aggressor in a military sense against any country having diplomatic relations with the United States or (2) using funds, of any sort, from the United States for purposes antagonistic to the foreign policies of the United States.

The President is also to consider terminating assistance, including that under P.L. 480, to any country which permits, or fails to take adequate measures to prevent, damage to U.S. property within such country, or fails to take appropriate measures to prevent the recurrence thereof and to provide adequate compensation for the damage.

Likewise, sales may not be made to countries with which the U.S. is not, at the time, maintaining diplomatic relations.

The Commodity Credit Corporation cannot finance a P.L. 480 program if the U.S. exporter is, or has recently been, engaged in business transactions with North Vietnam.

Excess military spending by recipient.--Before permitting sales to be made under this act the President is to take into account (1) the percentage of the recipient country's budget which is devoted to military purposes, (2) the degree to which the purchasing country is using its foreign exchange resources to acquire military equipment, and (3) the amount spent for the purchase of "sophisticated" weapons. The President must report annually to Congress on his actions in carrying out this program.

Expropriation of U.S. private property.--Termination of P.L. 480 assistance is required for any country which has expropriated U.S. private property without taking appropriate steps for payment, or arrangement for payment, of adequate compensation within a reasonable period of time.

Self-help provision.--Before entering into an agreement, consideration is given to the extent to which the recipient country is undertaking self-help measures to increase per capita production of food and to improve the means for storage and distribution of agricultural commodities. Each P.L. 480 agreement must contain a description of the self-help measures which the recipient country is undertaking. At least 20 percent of the foreign currencies set aside by a P.L. 480 agreement, for purposes other than those in section 104 (a), (b), (e), and (j), must be allocated for the self-help measures specified in the agreement. An exception to this provision is made for countries which are fighting Communist military forces.

The principle of "self-help" became an integral part of P.L. 480 in 1966 when nine self-help measures focusing on land use, infrastructure, research, education, public investment, and policy were incorporated into the law. In 1968, an amendment on voluntary programs to control population growth was added to the self-help list. The law specifies that each P.L. 480 agreement shall provide for termination of such agreement whenever the President finds

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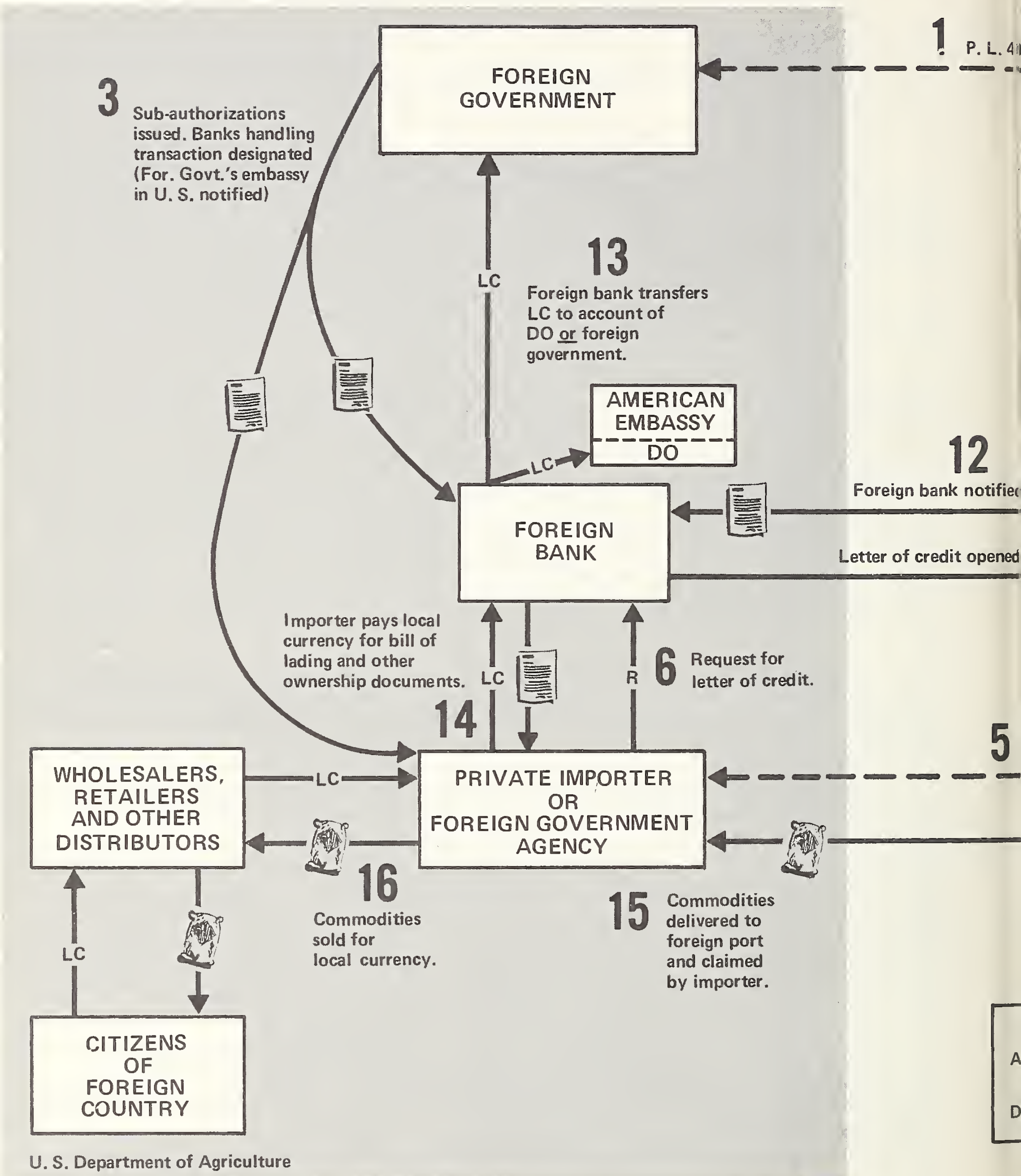
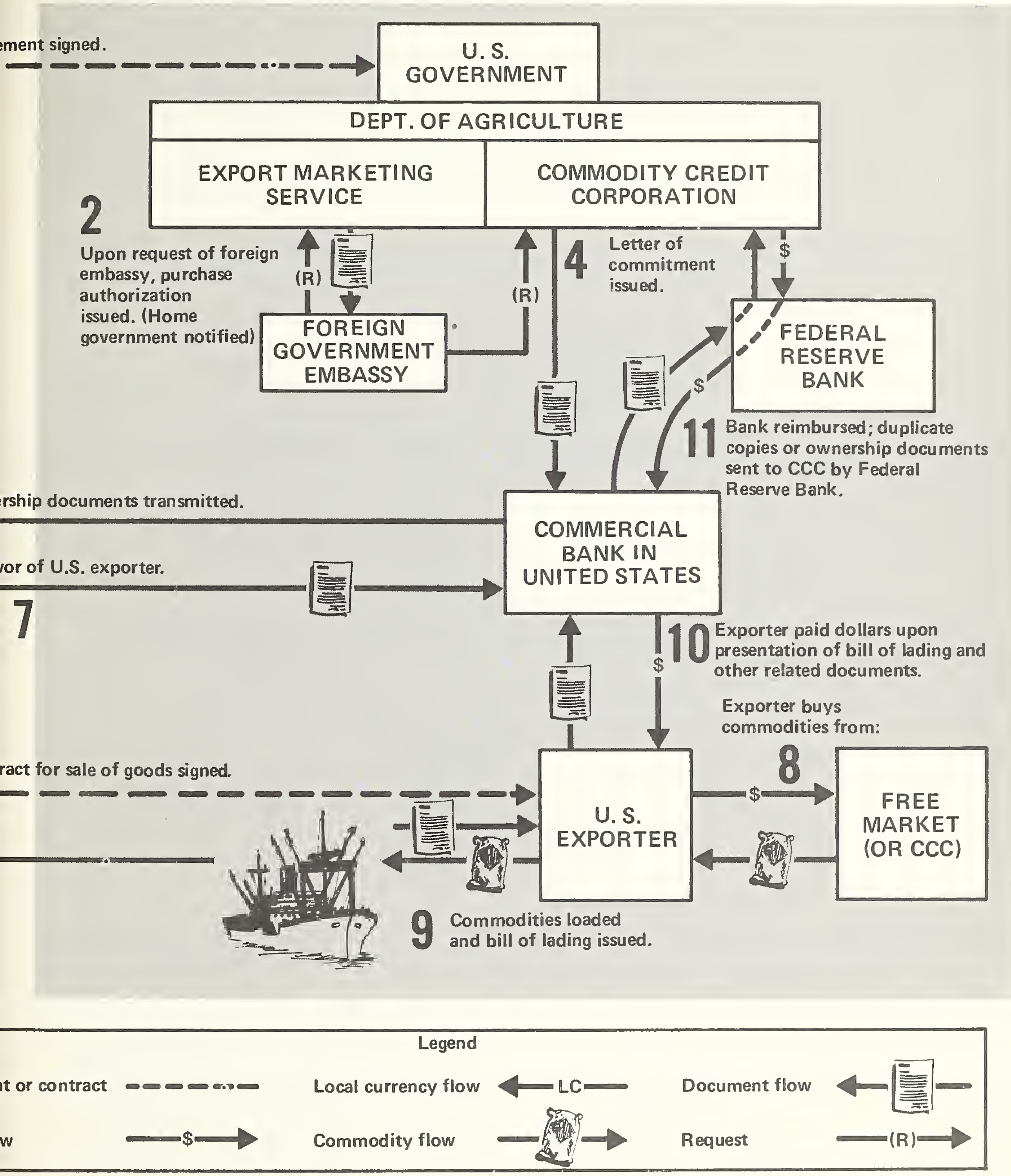


Figure 3. See

NCIAL OPERATIONS



ERS 7802 70(7)

that the self-help program described in the agreement is not being adequately developed.

IMPLEMENTATION OF SALES AGREEMENTS

The following narrative gives the sequence of events in the implementation of a P.L. 480 sales agreement under Title I, government-to-government agreements. Numbered paragraphs correspond to numbers shown on figure 3 which depicts the relationship of the various entities involved. For the most part, the following procedures also apply to private trade credit agreements. When the procedure for a PTE is significantly different, this difference is noted.

1. Signing the agreement.--The first step in the implementation of a sales agreement under Title I of P.L. 480 is the negotiation of the agreement, incorporating all the items discussed above. Following all adjustments and discussions between the two governments, a final version of the agreement is signed by representatives of the two countries.

2. Purchase authorization.--The government of the importing country applies (through its embassy in the United States) to USDA's Export Marketing Service for authorization to purchase agricultural commodities. When the embassy of the purchasing country receives a purchase authorization (PA), it notifies its home government so that appropriate action in the recipient country can be taken.

The PA is a document which specifies the particular grade or type of commodity to be purchased, the approximate quantity, the maximum dollar amount, the periods during which contracts between importers and (U.S.) exporters may be entered into, the amount of initial payment required, and the timespan during which deliveries must be made. The PA is more specific and limiting than the P.L. 480 sales agreement. The agreement may, for example, describe the import merely as "wheat," while the PA will stipulate "U.S. No. 2 or better Hard Red Winter Wheat." Each PA receives a number which must appear on all further documents concerning the transactions.

Purchase authorizations are issued periodically, usually for only a part of the total amount of one of the commodities called for in the agreement. PA's are not issued if P.L. 480 shipments disrupt world prices of agricultural commodities and normal commercial trade. Such things as the availability of port facilities and ocean shipping are carefully considered. Purchase authorizations may be withheld if a review of the program indicates that the recipient country is not abiding by the terms of the agreement, or if general economic and political conditions change so greatly that a reconsideration of the entire program is deemed necessary.

For private trade sales agreements, PA's are also timed to coincide with the needs of the project that was specified in the agreement.

USDA issues a public announcement each time a purchase authorization is issued. U.S. exporters are thus encouraged to participate in the program.

3. Subauthorization.--The government of the importing country may issue a subauthorization to a private importer (or importers) to purchase commodities pursuant to the provisions of P.L. 480 regulations and the purchase authorization. If private importers are not used, an agency of the country's government acts as the importer. At the same time that the recipient country's government designates an importer it will designate a bank or other agency in that country as "approved applicant" and a bank (or banks) in the United States to handle all transactions. The approved applicant (foreign bank) may be the central bank or a commercial bank; if a commercial bank is chosen it usually has a correspondent relationship with the designated American bank. Sometimes the government of the importing country will appoint one of its own agencies as the approved applicant rather than a bank. These agencies are sometimes located in the United States and in such cases the U.S. bank can contact them quickly and easily when necessary. There are other special reasons for appointing an agency rather than a bank. For simplicity, however, it is assumed in the remainder of this section that a foreign bank is the approved applicant.

4. Letter of commitment.--The importing country, through its embassy in the United States, requests CCC to issue a letter of commitment to each U.S. bank designated to handle transactions. The letter of commitment names the approved applicant, the U.S. commerical bank, and the Federal Reserve Bank which is to act as the agent of CCC. It constitutes a firm commitment by CCC to reimburse the U.S. bank for payments made, or drafts accepted, under letters of credit issued by the foreign bank. The letter of commitment stipulates that the U.S. bank must submit to CCC the appropriate documents required by P.L. 480 regulations and by the purchase authorization. After the U.S. bank accepts the letter of commitment, a copy is forwarded by CCC to the foreign government's embassy.

5. Sales contract.--The designated importer contracts with a U.S. exporter for purchase of the commodity. The importer may choose his supplier by any criterion he wishes, but must inform him that the transaction is taking place under P.L. 480 and must acquaint him with the terms of the purchase authorization. The contract price, mutually agreed upon by the importer and supplier, must not exceed the prevailing range of export market prices which is determined by USDA. Compliance with this regulation is verified by USDA. For all commodities, the exporter is required to submit the contract to USDA for review and approval at the time of sale. As indicated in step 10 below, the exporter must present the signed price approval notice, along with other required documents, to the U.S. bank to receive payment.

6. Request for letter of credit.--The importer applies to the designated bank in his country for a letter of credit in favor of his chosen supplier in the United States. A letter of credit is a financial document issued by a bank which agrees to honor drafts drawn upon it by a specified person, usually the exporter, under certain stated conditions (e.g., in exchange for a bill of lading and other documents). If an initial payment is included in the sales agreement, two letters of credit are often requested--one for the portion of the commodities to be financed by CCC and one for the portion to be financed by the importer. In some cases both portions are covered under one letter of credit.

7. Letter of credit issued.--The letter of credit is issued by the foreign bank and confirmed or advised by the U.S. bank. A "confirmed" letter of credit constitutes a commitment of both the issuing bank and the confirming bank that payment will be made if the terms of the credit are met. An "advised" letter of credit constitutes a commitment by the issuing bank only. Both types of credits must be irrevocable and as such cannot be canceled or altered prior to their expiry dates without the consent of the beneficiary. Irrespective of the type of credit, CCC is committed to reimburse the U.S. bank for eligible payments made thereunder. CCC is not committed to reimburse the U.S. bank for the portion of the sale covered by the initial payment.

After a letter of credit has been confirmed or advised by the U.S. bank, the bank notifies the exporter that he may draw upon an account established for this purpose, if he does so under the conditions stated in the document.

8. Purchase of commodities.--The exporter buys the commodity from regular commercial sources or from CCC.

9. Loading and shipping commodities.--The importer arranges for ocean shipping if commodities are to be shipped on an f.o.b. or f.a.s. basis (free on board; free along side). If the shipment is to go c. and f. or c.i.f. (cost and freight; cost, insurance, freight) the vessel is booked by the U.S. supplier. In any case, the shipping company delivers a bill of lading to the exporter when the items are loaded.

A bill of lading is a receipt for the commodities loaded on board, signed by the ship's master or other duly authorized person. It is a document of title of ownership to the goods described in the bill. This document subsequently passes from one entity to another as described below. It may serve as evidence of the terms of carriage agreed upon.

The Cargo Preference Act, discussed on page 15, applies to P.L. 480 shipments.

10. Exporter is paid.--The exporter presents the bill of lading, weight and inspection certificates, and other required documents to the U.S. bank. He receives payment, in dollars, at the price agreed upon in the sales contract and within the terms of the letter of credit previously received.

11. U.S. bank transactions.--The U.S. bank presents the documents required by CCC to the Federal Reserve Bank named in the letter of commitment. The Federal Reserve Bank, acting as the agent of CCC, pays dollars to the U.S. bank, or credits its reserve account.

12. Foreign bank notified.--The U.S. bank notifies the foreign bank of the transaction and transmits the original negotiable bill of lading and other documents.

13. and 14. Foreign bank and importer transactions.--Upon receipt of the bill of lading, the foreign bank notifies the importer. From step 1 to this point the procedures as stated above are the procedures followed regardless of the type of sales agreement. However, in these two steps, the procedure depends upon the type of sales agreement signed.

Under a local-currency sales agreement, the foreign bank is required to transfer local currency to the account of the U.S. or Regional Disbursing Officer (USDO or RDO) immediately upon receipt of documentation from the U.S. bank. This constitutes payment to the United States. The subsequent use of these currencies is discussed below in the section, "Local Currency Transactions".

The USDO is generally a State Department official attached to the American Embassy who is charged with the responsibility of administering local currencies according to Treasury regulations and directives. The RDO handles accounts for the United States in several countries within a particular geographic region. The bank used by the disbursing officer may or may not be the one which directly engages in the P.L. 480 transactions.

As noted above, the act requires in determining the number of local currency units to be deposited that the exchange rate used must be "not less favorable than the highest of exchange rates legally obtainable in the respective countries and which are not less favorable than the highest of exchange rates obtainable by any other nation." Countries with unitary exchange rates will, of course, present no problem in this respect. In any case, the deposit rate must be that rate of exchange which is in effect on the date of dollar disbursement by the U.S. bank.

Under an agreement where the terms are government-to-government dollar credit or convertible local currency credit, the importer pays local currency to his government through the designated bank. The bank transfers these funds to the account of the recipient government. (These are counterpart funds since they do not belong to the United States. The bank used by the recipient government may or may not be the approved applicant.) The government must then pay dollars in subsequent years as required by the sales agreement, or, in the case of a CLCC agreement, local currencies if the United States so desires.

The procedure for a credit sales agreement that contains provisions for a currency use payment are the same with one exception. Immediately upon delivery of the commodities, the foreign government makes available to the U.S. Government local currencies equal to the CUP provision rather than paying dollars at a later date.

Under a private trade dollar credit sales agreement, the PTE obtains the bill of lading without delivery of local currency to the bank, since it incurs a debt obligation to the U.S. Government in dollars. In this case, the foreign bank issues the letter of credit which governs the financing and it examines all documents received for conformity to the terms of its letter of credit.

15. Importer claims commodities.--Upon receipt of the bill of lading, the importer uses it to claim the goods when they arrive from the United States.

16. Distribution of commodities.--The importer makes final sale of the commodity within the recipient country through normal commercial channels. If the importer is a Government agency or a State trading corporation (as is often the case), it may decide to stockpile the commodities for eventual distribution in time of need.

This section explains the flow and administration of local currencies after they have been paid to representatives of the U.S. Government in the recipient country. Included within this discussion is an explanation of the accounting symbols and the classifications of currencies used by the Department of the Treasury. A knowledge of these is helpful in using Treasury or other Government publications reporting on collections, expenditures, or availability of local currencies.

Not all movements of currencies generated by P.L. 480 are discussed since most movements can be followed easily by reviewing figure 4. Furthermore, not all accounts associated with P.L. 480 are shown in figure 4. Over the years, some accounts were created for isolated situations and their inclusion in the figure would not add substantively to a general understanding of the procedures. In addition, the Department of the Treasury has a number of foreign currency accounts not associated with P.L. 480 and therefore not discussed here. Generally speaking, the procedures followed in handling other funds are similar to those followed in handling P.L. 480 funds.

Most of the accounting procedures used are not specified in P.L. 480 itself, but are the result of administrative decisions made in executing the law.

The discussion on the flow of local currencies is divided into three parts: (1) The flow into the disbursing officer's holding account, (2) movement into the program and sales account and (3) final distribution.

Disbursing Officer's Holding Account.--In figure 3, step 13, the foreign bank which holds the account of the USDO or RDO credits that account with the local currencies generated by the sale of commodities under a P.L. 480 LC sales agreement. In the accounting system of the U.S. Government, these funds move into a Treasury holding account number 20 FT 680, a special "collection" or "master" account. Prior to fiscal year 1965, some local currencies were guaranteed against loss of value through devaluation by a maintenance-of-value clause in the sales agreements. This clause required that the foreign government make a supplemental deposit sufficient to compensate for any loss of value that may have occurred between the time of deposit and the time when the funds were drawn out of the holding account. The account for such funds is 20 FT 690. This guarantee has not been included in recent agreements.

The first two numbers in Treasury's account symbols refer to the agency that has administrative control over the currencies. The agencies involved with P.L. 480 currencies and their account numbers are: Treasury (20), AID (72), HEW (75), and Defense (97). The letters FT stand for Foreign Transactions and mean that funds were obtained by the U.S. Government without being purchased with dollars. The last three digits are referred to as the "main" part of the specific account number. Various types of accounts fall within a specific range of numbers.

The Treasury Department has custody of and is responsible for the accounting for all foreign currencies received under P.L. 480. The deposits are audited by CCC which certifies the amount of local currency and U.S. dollars involved, and other particulars. After certification, transfer authorizations

MOVEMENT OF FOREIGN CURRENCIES GENERATED BY P.L. 480

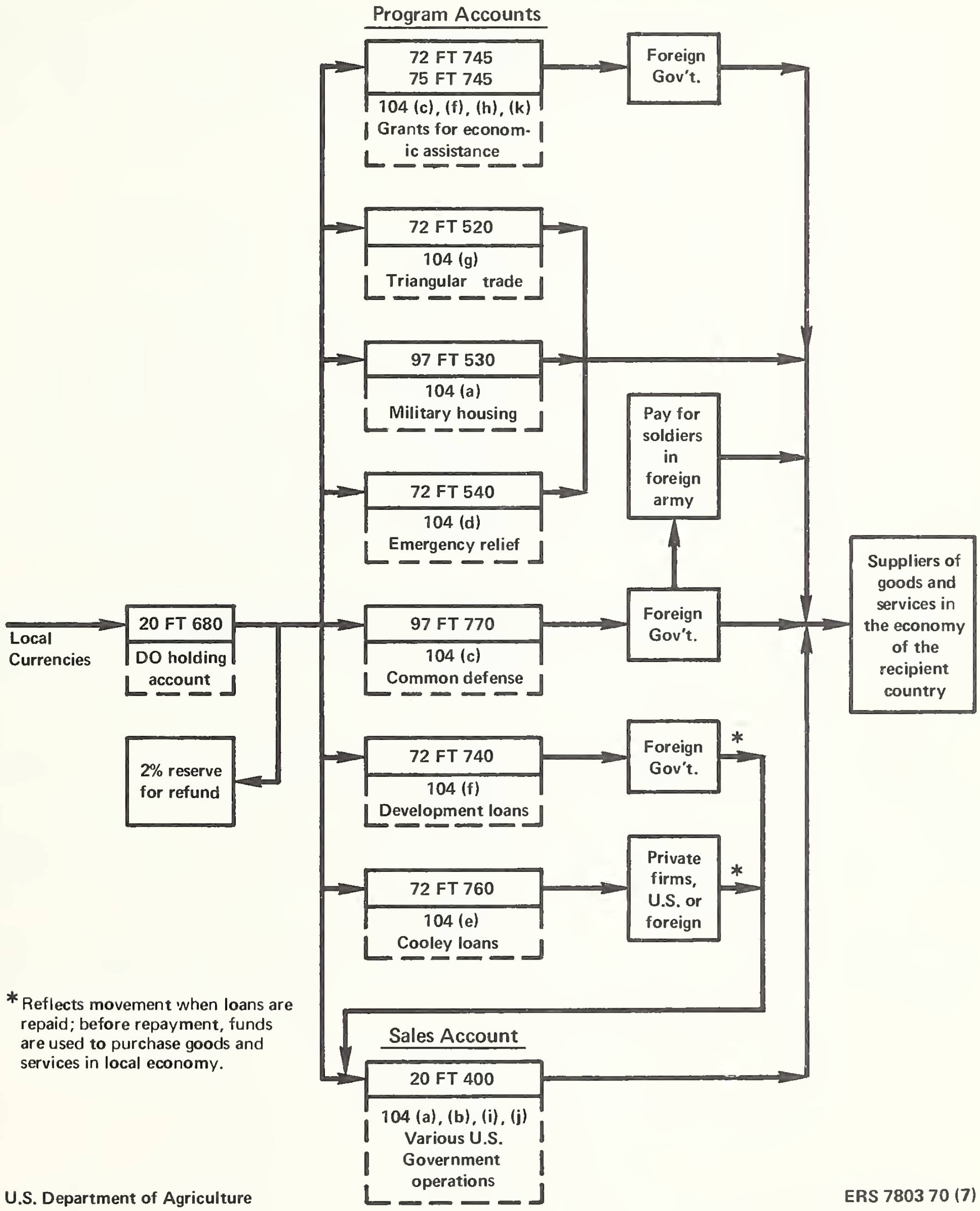


Figure 4

are issued by the Treasury Department to distribute the currencies according to the terms of the LC sales agreement. A refund reserve is maintained in the collection accounts (usually 2 percent) to satisfy claims for refunds caused by shortages, spoilage, etc. Thus, all currencies (except for the refund reserve) are transferred, generally once a month, from the collection accounts to agency accounts for use in various programs.

Program and sales account.--Figure 4 shows that there are at present seven program accounts and one sales account into which funds typically move. The funds in these accounts are classified on four different basis. They may be:

(1) restricted, nonrestricted, or reserved;
(2) for U.S. or country use;
(3) available to U.S. agencies with or without appropriated dollars; and
(4) excess, near-excess, or nonexcess currencies.

There is generally an interrelationship among the various basis of classification, but this relationship is not always a simple or uniform one. The classifications are the product of legal requirements and administrative decisions made through the years to meet various U.S. international and domestic objectives. While these legal provisions and administrative decisions were necessary to meet these objectives, they created a complex set of procedures for the administration of local currencies. The following discussion describes these classifications and gives an insight into the flow of local currencies.

Funds in the program accounts are classified as restricted since they can be used only as specified in particular subsections of section 104, P.L. 480. These subsections are indicated below each account symbol in figure 4 and are spelled out in appendix A. In practice, funds under a given agreement or in a given country are not necessarily used for all of the possible purposes. Local currencies transferred to the sales account (20 FT 400) can be used to meet any official obligation of any U.S. Government agency with operations in the recipient country. This is in accordance with subsection 104 (a) and such funds are referred to as nonrestricted funds. Funds for some specific programs--104 (b), (i), and (j)--are also transferred to this account. Reserved currencies are discussed below.

Figure 4 shows that funds for several purposes may be transferred into a single account, and conversely, funds for one purpose may be transferred into several accounts. There is therefore no one-for-one relationship between 104 subsections and Treasury accounts.

Funds in the program accounts may be:

(1) spent by the U.S. Government;
(2) lent to the recipient government or to private firms in the recipient country;
(3) granted to the foreign government, or
(4) left unused in the account.

The last is an unintended use but one that occurs and that has monetary and financial implications equal in importance to the other dispositions.

The classification of funds as U.S.-use or country-use is determined by who administer the funds at the point they are used to purchase goods and services and not, as the title may imply, who is the ultimate recipient or beneficiary. Funds in sales or program accounts that are spent by the U.S. Government are U.S.-use, although the benefits to the United States may be political, moral, or humanitarian rather than economic. Funds used for 104 (d), emergency relief, and 104 (i), programs to help improve agricultural practices in recipient countries, are classified as U.S.-use currencies. U.S.-use currencies are restricted if in program accounts and nonrestricted if in the sales account.

Prior to 1963, currencies were quite often transferred to restricted U.S.-use accounts even though they were not needed at that particular time by the agency for which they had been set aside. While large amounts of such currencies were lying idle in some accounts in some countries, the United States often needed local currencies for other operations. Since such currencies were not available from P.L. 480 operations, the United States had to obtain them by purchase with dollars from commercial sources. This worsened the U.S. balance of payments; so, a law passed on December 31, 1963 established procedures to free idle funds. Agencies possessing such currencies are issued Foreign Currency Reservation Certificates to compensate for the currencies surrendered. These certificates authorize the agencies that have surrendered currencies to buy local currencies from the sales account when they subsequently need currencies and as their budgets permit. If the DO's supply of local currencies is depleted because of other uses, he is required to go into the local money market and purchase the necessary amounts of local currencies with dollars. Reserved currencies are those against which Foreign Currency Reservation Certificates have been issued.

Funds to be lent or granted by the U.S. Government are classified as country-use currencies. The detailed administration of these funds is outside the direct control of the U.S. Government at the time they are used to purchase goods and services. However, the United States exercises indirect or general control by establishing limitations and restrictions on the use of these funds. Nearly always, country-use currencies are spent for the direct benefit of the recipient country although (1) there is no legal requirement that this be the case, and (2) the benefit may be mutual as in the case of grants under 104 (c) for common defense.

By its very nature, the sales account contains only unrestricted U.S.-use currencies. On the other hand, program accounts taken as a group may or may not contain U.S.-use currencies. Accounts established for U.S.-use have been assigned numbers in the five-hundreds for the main part of the account symbol. For country-use, the seven-hundreds are used.

Since the inception of P.L. 480, a little over 25 percent of P.L. 480 currencies have been U.S.-use and about 75 percent country-use (table 2). Whether U.S.-use or country-use, all funds generated under P.L. 480 local currency sales are U.S.-owned and thereby differ from counterpart funds. Counterpart funds originated during the 1940's and are generated principally by grant

Table 2.--Cumulative value of agreements and collections under P.L. 480, by agreement terms, 1954 to mid-1969

Agreement terms	Agreement provisions	Cumulative collections as earmarked for programs 1/	
		Value	Percentage of total
	Million dollars	Million dollars	Percent
U.S.-use, total	2,854	3,118	25.6
Original distribution	---	2,671	22.0
Released from other uses	---	447	3.7
Country-use, total	10,443	9,038	74.3
Loans, total	7,004	5,871	48.3
104(e)	766		3.7
Original distribution	---	682	5.6
Released to other uses	---	-232	-1.9
104(f)	6,238	5,421	44.6
Original distribution	---	5,648	46.4
Released to other uses	---	-227	-1.9
Grants, total	3,440	3,169	26.1
104(c)	1,508	1,376	11.3
Original distribution	---	1,374	11.3
Released from other uses	---	2	2/
104(f)	1,888	1,763	14.5
Original distribution	---	1,752	14.4
Released from other uses	---	11	.1
104(h)	42	29	.2
104(k)	2	1	2/
Reserved for refund	---	1	2/
Suspense	---	3	2/
Grand total	13,298	12,160	100.0
Memorandum:			
In holding accounts	---	469	3.9

1/ Includes ocean transportation.
2/ Less than 0.05 percent.
Reproduced from: U.S. Treasury Department; Semiannual Report of Collections Under Title I, P.L. 480 Sales Agreements, June 30, 1969.

aid. They are owned by the recipient country but the United States can veto a proposed use of the funds by the foreign government. Under certain limited situations a portion of counterpart funds may be transferred to U.S. accounts to meet U.S. needs in particular countries.

Local currencies in the sales account are available to U.S. agencies in exchange for dollars that have been appropriated by Congress for specified programs. As the currencies are used to pay obligations, the particular dollar appropriation involved is charged with the dollar equivalent of the currencies used, usually at the prevailing bank rate of exchange. At the same time CCC's revolving fund is correspondingly credited, thereby partially reimbursing CCC for its initial dollar outlays in acquiring and shipping the commodities. U.S. Government agencies reimburse CCC monthly as they utilize the foreign currencies to pay for their programs in lieu of spending U.S. dollars abroad.

Currencies in all program accounts which are related to P.L. 480 are generally available without dollar appropriations, whether U.S.-use or country-use currencies. Thus, CCC is not reimbursed for commodities furnished to the P.L. 480 program to the extent that local currencies are allocated to program accounts--excepting for the moment the eventual repayment of 104 (f) development and 104 (e) Cooley loans, and from the interest on such loans.

A particular currency is designated an excess currency by the Treasury Department where the supply owned by the United States and available for use by it is determined to be in excess of normal requirements of agencies of the United States for expenditues in that country for the two fiscal years following the year in which the determination is made. This designation permits agencies to request reservations of the currency for expenditure under appropriations for "special foreign currency programs" which utilize excess currencies exclusively. The excess-currency countries during fiscal year 1969 were Burma, Ceylon, Guinea, India, Israel, Morocco, Pakistan, Poland, Tunisia, United Arab Republic, and Yugoslavia. Where the supply of currencies is above the immediate needs of the U.S. Government, but not sufficient to be declared excess, the currency is designated a near-excess currency by the Treasury Department. The near-excess currency countries during FY 1969 were Bolivia, Ghana, Indonesia, and Sudan. The currencies of the other countries (about 73) are called nonexcess currencies, indicating that the nonrestricted U.S. holdings are not expected to exceed requirements for the reasonable, foreseeable future. In most nonexcess currency countries, the U.S. Government must purchase currencies with dollars from commercial sources for part or all of its operating requirements.

Final distribution.--In lending local currencies to a foreign country, the terms are included in loan agreements which establish lines of credit up to the amounts stipulated in the sales agreement. The loan agreements state the rate of interest to be charged and provide that loans may be repaid in dollars or in the currency of the borrower. Terms of loans vary considerably although minimum terms are set by law. The policy governing them is set by the National Advisory Council on International Monetary and Financial Policies (NAC), and the policy has been revised from time to time. Even without this influence, financial conditions vary so greatly from country to country that the only generalization possible is that the terms are tailored to fit the conditions in the respective countries.

Repayments of loans and payments of their interest flow into the sales account and, as indicated in figure 4, they can be used for the purposes stated in subsections 104 (a), (b), (i), and (j). In excess and near-excess currency countries, payments of principal and interest can be transferred from the sales account to any program account. To accomplish this, however, an agency must request such a transfer from the Bureau of the Budget.

Currencies for 104 (g), triangular trade, are set aside in account 72 FT 520. From this account they are used to purchase commodities which are exported to a "third" country. In the third country, these goods are sold for the currency of that country and the payments flow into the sales account established there. From this point onward these funds are treated like any other funds in a sales account.

Funds do not remain indefinitely in program accounts. If they are not used within 3 years after a particular agreement has been signed, they are usually transferred to the sales account.

REAL AND MONETARY EFFECTS OF LOCAL CURRENCY TRANSACTIONS

As already stated, the primary objectives of P.L. 480 are to develop export markets for U.S. agricultural commodities and to provide food to hungry people in foreign nations which do not have enough foreign exchange to purchase agricultural commodities in the international market. P.L. 480 is also used to help improve the U.S. balance of payments. To accomplish the objectives of P.L. 480, foreign nations are often permitted to make payments in local currencies. However these currencies may or may not help the U.S. balance of payments. These currencies do not possess all the characteristics that most moneys do. To a large extent they cannot be spent freely by the United States or exchanged for other currencies. The degree of inflation that occurs in some less developed nations causes these currencies to lose a basic characteristic of money--a store of value. And in some cases the expenditure of these currencies does not materially benefit the spender.

Thus local currency transactions sometimes have unusual effects. It is not always clear whether these transactions result (1) in a pure grant of food from the United States to the recipient country; or (2) whether they have an effect similar to a business transaction between two entities and thereby improve the U.S. balance of payments. This section describes which of these results is effected by spending, lending, granting, or leaving unused foreign currencies in the program and sales accounts described in the previous section.

We determined the effects of various transactions on the U.S. balance of payments. So statements are made, for example, that the United States (1) "receives quid pro quo" or (2) "suffers a loss" as a result of a particular transaction. Our intent is to show that the former transaction was more nearly a commercial one whereas the latter was a grant. The intent is not to imply that the United States should have undertaken the first and not the latter. For certainly it is U.S. policy to aid nations that are determined to help themselves.

Expenditures.--U.S. expenditure of local currencies in a recipient country can be viewed in several ways. If the goods and services purchased are of direct benefit and use to the United States, then by any reckoning the United States has received quid pro quo for the agricultural commodities shipped under P.L. 480. To this extent, a P.L. 480 transaction approaches that of a commercial transaction and therefore benefits the U.S. balance of payments.6/

If, on the other hand, the goods and services that are purchased with these currencies by the United States are for the direct benefit and use of the recipient country, as they often are, then the United States, in a narrow sense, has received payment for the P.L. 480 commodities, but at the same time it has returned the value of this payment to the recipient country. The United States, in real economic terms, lost when it delivered the P.L. 480 commodities, gained when it purchased goods and services with the local currencies generated, and lost again when it made available the benefit of these purchases to the recipient country. On balance, there was a transfer of real U.S. wealth from the United States to the recipient country. In short, the magnitude of the grant equals the value of the U.S. expenditure.

The real wealth transferred in this case can be considered either (1) the goods and services made available by the expenditure of local currencies under a particular aid or military program or (2) a quantity of P.L. 480 commodities equal in value to the local currency expenditure. In this context, it is obvious that to count both would be double counting, but this error is not always so obvious in some analyses of the effects of P.L. 480. With either interpretation, the effect is that P.L. 480 shipments make a grant possible without an outflow of dollars. In fact P.L. 480 shipments represent in effect 100-percent tied aid, that is, aid given with the stipulation that the commodities purchased with the money lent or granted be produced in the country granting the aid.

The P.L. 480 program also makes it possible to transfer goods and services from one sector of the recipient country's economy to another. The United States sometimes uses local currencies to purchase goods and services from one sector while the item purchased is used to benefit another. Since only a shifting of resources within an economy occurs, and not an addition to its resources, the real grant to the recipient country is, in the final analysis, the P.L. 480 commodity.

Expenditures of local currencies also have an indirect but meaningful effect on U.S. congressional appropriations to CCC. As stated above, U.S.

6/ For a discussion of the inflationary impact on the recipient country and the balance of payments impact of local currency and dollar credit sales on the United States and the recipient country, see: Elrod, Warick E., "Monetary Effects of Financing Agricultural Exports", U.S. Dept. Agr., For. Agr. Econ. Rpt. 12, Nov. 1963. For a measurement and an analysis of the problems of measuring the impact of P.L. 480 on the U.S. balance of payments see: Kruer, George R., "U.S. Agriculture and the Balance of Payments, 1960-67," ERS-Foreign 224, Apr. 1968.

agencies that have overseas programs can make purchases with local currencies generated by P.L. 480. The dollars they use to purchase these currencies are credited to CCC's revolving account No. 12 X 4336. The dollars CCC receives in this manner thereby lessen the need for direct appropriations to reimburse CCC for the cost of the P.L. 480 program.

The flow of local currencies, dollars, and agricultural commodities is shown in figure 5. Local currencies do not actually flow into and out of an account established for a U.S. agency as shown in steps 5 and 6, but in effect this occurs and for analytical purposes the in-and-out flow is shown. In real terms, a foreign nation pays for the farm commodities it receives with goods and services it provides over time. The dollars a farmer receives may have been appropriated by Congress for overseas expenditures, such as construction of military bases or embassy facilities. The figure shows how the U.S. agency receives the local goods and services for which Congress has appropriated dollars even though the dollars were paid to CCC. The inflow and outflow of local currencies into the U.S. agency account offset each other and on balance the agency pays dollars for the goods and services it receives abroad even though the dollars go to CCC rather than the foreign nations. However, the net effect on CCC's position is not necessarily zero, since CCC may have to pay interest on the money it has used to purchase the commodities programed under P.L. 480.

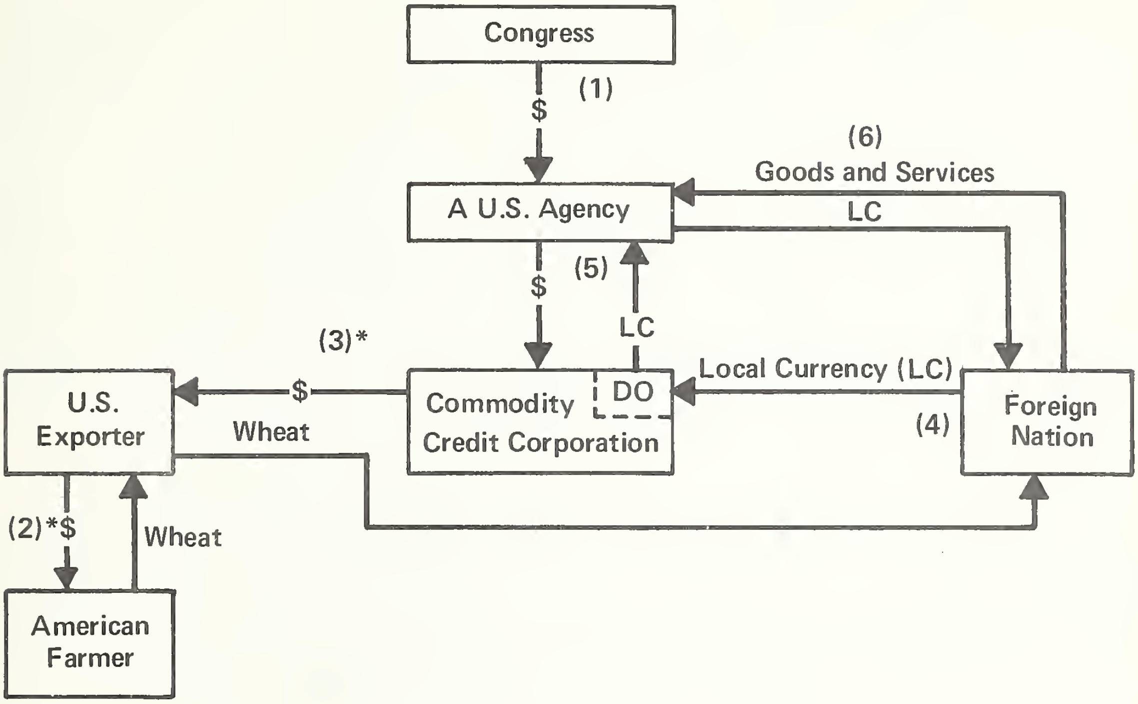
Furthermore, CCC has not received many dollars by this route--only $1,947 million or 11 percent of the $17,037 million gross cost to CCC of financing sales of agricultural commodities for foreign currencies from July 1, 1954, through December 31, 1968. The gross cost includes $15,650 million for commodities and related cost, $1,140 million for ocean transportation (including $624 million for ocean freight differential) and $247 million for interest. Except for ocean transportation cost, most of the CCC cost occurred originally under the U.S. price support program.

The $1,947 million of local currencies purchased by U.S. agencies from CCC represents a U.S. balance of payments benefit if the agency's expenditures abroad would have occurred in the absence of the availability of P.L. 480 local currencies.

Loans.--Local currencies lent to a recipient government or private firms in the recipient countries are spent by the borrower in that particular economy. When principal and interest are paid on these loans, the funds enter the U.S. sales account. From there, they may be used to obtain goods and services for any official purpose and thereby benefit the U.S. balance of payments.

From the beginning of P.L. 480 in July 1954 to June 30, 1969, the equivalent of $5.2 billion had been lent. Of this, $0.3 billion equivalent had been repaid and interest collections totaled just under $0.7 billion. However, due to inflation, the purchasing power of currencies lent depreciated by more than $0.8 billion. This value was measured by the devaluation of currencies, which may not fully reflect the loss of purchasing power. Thus, in real terms, the United States has granted, through this means alone, more than $0.8 billion of agricultural commodities under the P.L. 480 program.

RELATION OF CONGRESSIONAL APPROPRIATION TO THE FLOW OF AGRICULTURAL COMMODITIES AND LOCAL CURRENCIES UNDER A P.L. 480 PROGRAM



1. Congress appropriates dollars for overseas programs conducted by the Departments of Defense, State, and others.

2. U.S. exporter, in preparation for shipment under P.L. 480, purchases wheat from an American farmer.*

3. Commodities are shipped and exporter is paid in dollars by CCC from its revolving fund.*

4. Foreign nation receives commodities and makes payment in local currencies to CCC. The Disbursing Officer collects and administers these funds as an agent for USDA.

5. With appropriated dollars, a U.S. agency, in effect, buys local currencies from the Disbursing Officer and the dollars are credited to the CCC.

6. The local currencies are used to purchase local goods and services.

*Exporter sometimes buys commodities from CCC stock in which case the farmer receives dollars directly from CCC rather than through the exporter.

U.S. Department of Agriculture | ERS 7804 70 (7)

Figure 5

After reducing the $5.2 billion worth of loans by the $0.3 billion repayment and $0.8 billion writeoff, there remained $4.1 billion worth of loans outstanding, as of mid-1969. Of this, only $0.9 billion is protected by maintenance-of-value clauses included in the various loan agreements. The remaining $3.2 billion is subject to indirect granting through loss of value due to inflation.7/

Grants.--As table 2 shows, nearly $3.2 billion has been made available for grants from the beginning of P.L. 480 to mid-1969 and all but $0.1 billion had actually been granted. By itself, the granting of these currencies does not transfer real wealth to the recipient economy. It transfers the control over resources already in the recipient country from the U.S. Government to the government of the foreign country. This control, of course, was originally in the hands of the citizens of the country before they exchanged it (in the form of their currency) for P.L. 480 commodities. The government could have obtained control through taxation or other means but these may not be economically, politically, or administratively feasible in many less developed nations. Thus the P.L. 480 program in this context becomes a useful technique of obtaining development resources without recourse to taxation. An opposing view could be taken that there is in fact taxation, but the impact on the individual is softened since he is given food equivalent in value to the tax.

To the extent currencies are granted, the United States loses all possibility of receiving quid pro quo for the P.L. 480 commodities exported. In this sense, and to this extent, P.L. 480 shipments do not contribute to the U.S. balance of payments in the way that commercial exports do. The granting of local currencies can be viewed as a measurement of the grant aid involved in shipments of P.L. 480 commodities. These grants have the same effects as those that occur when the United States spends currencies for the purchase of goods and services for the direct benefit and use of the recipient country. There is, again, aid without a dollar outflow.

Dormant currencies.--Funds left unused in Treasury accounts beyond a reasonable length of time represent in real terms either loans or grants to the recipient country. Before distinguishing whether they are loans or grants, it is essential to note that the United States has delivered commodities and has received local currencies as payment. However, these currencies are not "money" in the full sense of the word since there are various limitations placed upon their use. The primary limitation is one of geography--the bulk of the funds must be spent within the recipient country. In some countries, however, the United States may have no need for these currencies for many years to come, and in some cases, perhaps never will. Since these currencies are not money in the full sense, they are not truly payments for the commodities and represent either (1) a loan while lying idle before eventually being used, or (2) a grant if never used. At the time the unneeded currencies are received, it is sometimes impossible to know whether they are one or the other since future U.S. currency needs may not be known.

If currencies left dormant in the sales account are eventually spent by the United States, then in the intervening period the local currencies can be

7/ Source of data: Agency for International Development, "Status of Loan Agreements, as of June 30, 1969", p. iv.

considered as evidence of a loan and also as measuring the magnitude of the loan. As with all debt instruments, there exists the chance of losing real purchasing power if inflation occurs. To the extent that this occurs, there is a grant in real terms from the lender to the borrower. Even with a maintenance of value clause, a loss of purchasing power ensues if inflation occurs without a devaluation or an insufficient devaluation. Of course, inflation at a rapid rate without devaluation is not tenable for very long.

Funds left in the sales account and never used can be considered a measure of the grant involved in a P.L. 480 program (or at least one part of the grant) since in real terms the United States never received quid pro quo for commodities delivered. One reservation is attached to this conclusion: In nearly all countries, the United States receives interest on all funds in the DO's account, even in excess-currency countries such as India. Thus, if the commodities, equal in value to the unused currencies, are considered a grant, the grant is an unusual one in that it draws interest. On the other hand if the "never-used" currencies are considered a loan, then it is a loan where the principal, in real terms, is never collected and used. But if the original funds are never to be used, neither will the currencies received as interest. So, it is probably best to consider funds never used as a measure of the grant involved.

Funds left in program accounts for development loans, or loans to private enterprise, which are eventually lent have the characteristic, under some circumstances, of being implicitly a loan while lying idle and explicitly a loan when they are formally lent. They are, in real terms, a loan if, when repaid, the United States has an eventual need for them. Otherwise, the funds measure the grant involved whether they are lying idle or are formally lent. Local currencies allocated to an account established for grants may or may not in reality be grants. If an agreement between the United States and the recipient country has not been reached within 3 years from the date of the sales agreement on the use of the funds, then they are returned to the sales account. This arrangement has been used since the mid-1960's and is also applied to accounts established for loans. If, after transfer to the sales account, the funds are eventually spent by the United States, the United States has delayed demanding payment for goods supplied. In real terms the United States has extended credit. On the other hand, if after returning to the sales account, the funds are never spent by the United States, a grant has been made whether or not the funds are formally granted. Thus, the recipient government is under no pressure to formally apply for the grant under most circumstances. That government may need revenues without taxation, but in most countries it can obtain it through its own monetary and banking institutions without recourse to U.S. funds. Such a procedure may be inflationary--but any expenditures of funds would be in a full employment situation--whether the funds came from unused balance or were newly created.

This glossary has been prepared for those who are not familiar with the P.L. 480 program (or those who only occasionally use it) to give a working knowledge of the concepts and terminology that have evolved over the years. Definitions are as brief as possible and therefore may not be sufficient from a legal point of view. All definitions were constructed in the context of the P.L. 480 programs with the consequence that they may or may not be accurate in another context.

1. Cargo preference.--In 1954, the Cargo Preference Act (P.L. 83-664) added section 901 (b) to the Merchant Marine Act of 1936; this amendment requires that at least 50 percent of the volume of P.L. 480 commodities be shipped in U.S.-flag vessels, if such vessels are available at reasonable rates for U.S. flag vessels. This law applies to concessional sales financed under certain other Government programs as well.

2. Compliance (convertibility and payments).--The status of a P.L. 480 recipient country with regard to foreign currency convertibility and debt payment required by previous agreements. A country is in compliance as to convertibility and payment requirements if it has been timely in meeting the convertibility and payment provisions specified in agreements.

3. Compliance (usual marketing requirement).--The status of a P.L. 480 recipient country in regard to the usual marketing requirements of previously signed agreements. A country is in compliance as to usual marketing requirements if it has imported the quantity (or sometimes value) of the commodities specified by such agreements as part of its normal commercial imports.

4. Commodity Credit Corporation, (CCC).--A corporate body and a U.S. Government agency within the U.S. Department of Agriculture. It was created for the purpose of (1) stabilizing, supporting, and protecting farm income and prices, (2) assisting in the maintenance of balanced and adequate supplies, and (3) facilitating orderly distribution of commodities. CCC therefore engages in a number of agricultural export activities under its charter authority. It superintends U.S. operations under the International Grains Arrangement and finances the sale and export of commodities under P.L. 480.

5. CCC Cost.--The gross cost to the Commodity Credit Corporation of financing the sale and export of U.S. agricultural commodities under Title I, P.L. 480. This gross cost includes that portion of the cost of the commodities and ocean transportation financed by CCC.

6. Concessional sale.--A sale in which the buyer is allowed payment terms which are more favorable than those obtainable on the open market. Under P.L. 480, the concession may be the type of currency accepted as payment, the length of the credit and grace period, or the interest rate charged.

7. Convertibility requirement.--The requirement that local currencies acquired from local currency agreements be changeable into dollars or other currencies needed by the United States.

8. Convertible local currency credit sales (CLCC).--A credit sale in which installments can be paid either in dollars, or at the option of the United States, in currencies that can be converted into dollars. The payment period can extend to a maximum of 40 years.

9. Cooley loans.--(See loans to private enterprise)

10. Country-use currencies.--Foreign currencies accruing from P.L. 480 sales which are lent or granted to the recipient country. They are classified as country-use because they are administered by the recipient country at the point at which they are used to purchase goods and services.

11. Currency use payments (CUP).--The provision in credit sales agreements that local currencies be made available for U.S. use at the time of commodity delivery. This provision is not included in agreements when it is determined that it would be inconsistent with the objectives of the act. These payments may be considered advance payments of the earliest installments (of dollars) due under the agreement.

12. Dollar credit sale (DC).--A credit sale to be paid in dollars over a maximum of 20 years. Before 1967, the authority for these sales was in Title IV of the act, but it is now under Title I.

13. Excess-currency country.--A country in which the United States owns local currency in excess of its expected normal requirements in that country for 2 fiscal years following the year in which the determination is made.

14. Exchange rate, highest legally obtainable.--The highest legal exchange rate of dollars for local currency in the country with whom the United States has a P.L. 480 agreement. This rate must be no less favorable than that afforded any other country.

15. Export limitation.--A provision that limits the recipient country's volume of exports of commodities that are the same as, or like, the commodities being furnished by the United States under a P.L. 480 agreement. The export of the actual commodities financed is also of course prohibited.

16. Export limitation period.--The period during which the recipient country must restrict exports of commodities which are considered to be the same as, or like, those supplied under P.L. 480.

17. Export market value, total.--The market value of the commodity based upon world prices plus any ocean transportation cost included in financing arrangements.

18. Fair share.--The requirement that the United States should benefit equitably from any increase in commercial purchases of agricultural commodities by the recipient country.

19. Government-to-government agreement.--An agreement between the U.S. Government and a foreign government, as opposed to an agreement between the U.S. Government and a private trade entity.

20. Initial payment.--A payment to be paid by the importing nation in dollars, or currencies easily convertible into dollars, at the time of delivery.

21. Interagency Staff Committee (ISC).--The committee develops, and prepares, all proposed P.L. 480 programs and related negotiating instructions, which are subsequently transmitted to the appropriate U.S. ambassador. The ISC is chaired by a USDA representative and members include representatives of the Departments of Treasury, Commerce, State (including the Agency for International Development), and Defense, and the Bureau of the Budget.

22. Letter of conditional reimbursement.--A letter issued by the Department of Agriculture making a conditional commitment to finance the procurement of U.S. commodities by a recipient country. Initially, payment for the commodities must be made from that country's own monetary resources. The U.S. commitment is made in advance of executing an agreement. The letter obligates the United States to reimburse the importing country, or its assignee, for procurement accomplished subsequent to the letter but prior to the agreement providing that (1) the pending P.L. 480 sales agreement is eventually signed and (2) all requirements established by the letter of conditional reimbursement were met. To allow for the possibility that the sales agreement may require an initial payment, the letter further limits the reimbursement to the percentage of the total value approved for financing in the agreement.

23. Loans to private enterprise (Cooley loans).--Loans made from P.L. 480 local currencies in recipient countries to (1) U.S. firms (including their branches, affiliates, and subsidiaries) for business development, trade expansion, and private home construction, or to (2) domestic or foreign firms for the establishment of foreign facilities for aiding in the utilization distribution, or otherwise increasing the consumption of, and market for, U.S. agricultural products. These loans may be repaid in foreign currencies and usually bear interest at the going rate in the foreign nation where the loan is made. This program is administered by the Agency for International Development.

24. Local currency sale (LC).--A P.L. 480 Title I sale in which payment is made to the United States in the recipient country's currency at the time of delivery. Generally these currencies are not convertible.

25. National Advisory Council on International Monetary and Financial Policies (NAC).--An interdepartmental committee established by executive order and whose members are representatives of the Departments of Treasury, State, and Commerce, the Federal Reserve System, and the Export-Import Bank. Among other functions, it coordinates the policies of all government agencies to the extent that they make foreign loans or engage in foreign monetary transactions. Thus it reviews proposed P.L. 480 dollar credit and convertible local currency credit agreements.

26. Near-excess currency country.--A country in which the U.S. Government holds local currency in excess of the expected requirements of the U.S. Government in that country for a period of more than 6 months but less than 2 years from the date of determination.

27. Negotiating instructions.--Instructions drafted by USDA, cleared with interested U.S. agencies, and transmitted by Department of State-AID to the appropriate U.S. Embassy. They guide the Ambassador, or his designees, in negotiating a particular P.L. 480 sales agreement.

28. Ocean freight differential (OFD).--The amount by which (1) the cost of the ocean freight bill for the portion of commodities required to be carried on U.S.-flag vessels exceeds (2) the cost of carrying the same amount on foreign flag vessels. This amount is paid outright by CCC.

29. Private trade agreement (PTA).--A P.L. 480 agreement negotiated between the U.S. Government (USDA) and a private trade entity (PTE), either U.S. or foreign. The agreement provides that the PTE will export certain commodities to a particular country and execute projects in that country which will improve the storage or marketing of agricultural commodities or expand private economic enterprise. Financing of these agreements is restricted to dollar credit. The agreements are negotiated in Washington, D. C.

30. Private Trade Entity (PTE).--The private trader with whom the U.S. Government (USDA) directly negotiates a private trade agreement.

31. Purchase authorization (PA).--A document issued by USDA after a P.L. 480 agreement has been signed. It authorizes the importing government, through its importers or agents, or a PTE to procure certain P.L. 480 commodities from U.S. sources. The PA specifies the grade and type, approximate quantity, maximum value, the timespan for purchase and delivery of commodities; the method of financing; and certain other provisions and limitations. An individual PA can be issued for the total value of one of the commodities in an agreement or for part of the commodity total. A similar document is also issued for procurement of ocean transportation to be financed by CCC where applicable.

32. Same as, or like, commodities.--Some commodities, including certain processed products containing them, which are approximately the equivalent of commodities included in P.L. 480 agreements and which the recipient nation may be restricted from exporting. The "export limitation" and "export limitation period" apply to these commodities.

33. Self-help provision.--The provisions contained in each P.L. 480 agreement which describe the steps of a program which the recipient country is undertaking or agrees to undertake to improve the production, storage, and distribution of its agricultural commodities. An agreement may be terminated whenever the President finds the self-help program is not being adequately developed.

34. Title I sales.--Sales made under Title I of P.L. 480, which includes local currency, dollar credit, and convertible local currency credit sales. It therefore includes all sales under P.L. 480 except barter sales. Prior to 1967 the term "Title I" meant local currency sales, since only this type of sale was included under this Title.

35. Title IV sales.--Dollar credit sales, both government-to-government and private trade agreements, which were made under Title IV of the act prior to 1967. After 1966, all dollar credit sales provisions were transferred from Title IV to Title I.

36. Third-country consultations.--A review by the U.S. Government with the governments of countries which normally make commercial exports to the P.L. 480 recipient nation, or have available for export the same or similar commodities as those being considered for inclusion in an agreement. The purpose of the consultation is to assure the exporting countries that normal commercial trade will not be disrupted or displaced.

37. U.S.-use currencies.--Foreign currencies accruing from sales under P.L. 480 agreements which are used by the United States to purchase goods and services in the recipient country. The goods and services purchased do not necessarily benefit directly the U.S. Government.

38. Usual marketing requirement (UMR).--The amount of a commodity which the P.L. 480 agreement requires the P.L. 480 recipient nation to import on a commercial basis. This amount is normally based on the country's historical commercial imports of the commodity from countries friendly to the United States. Commercial imports can include items supplied under barter or short-term credit sales.

APPENDIX B. LOCAL CURRENCY USES

Under P.L. 480 agreements, many types of foreign currencies become the property of the U.S. Government. The purposes for which these currencies can be used are stated in the various subsections of section 104 of the act which are summarized below.

Subsection

(a) Pay U.S. obligations (including obligations entered into pursuant to other legislation).

(b) (1) Help develop new markets for U.S. agricultural commodities on a mutually benefiting basis.

(2) Finance international educational and cultural exchange activities under the program authorized by the Mutual Educational and Cultural Exchange Act of 1961, and a number of educational acts administered by the Department of Health, Education, and Welfare.

(3) Collect, translate, and distribute scientific and technological information; conduct research and support scientific activities overseas; and promote and support programs of medical and scientific research, cultural and educational development, family planning, health, nutrition, and sanitation.

(4) Acquire by purchase, lease, or otherwise, sites, buildings and grounds abroad for U.S. Government use, and construct, repair, alter, and furnish such buildings and facilities.

(5) Evaluate foreign publications; register, index, reproduce publications and acquire those of cultural and educational significance.

(c) * Procure equipment, materials, facilities, and services for the common defense, including internal security.

(d) Assist in meeting emergency or extraordinary relief requirements other than food commodities.

(e) * Provide loans to U.S. business firms or affiliates for business development and trade expansion abroad, and to domestic or foreign firms for increasing the consumption of, and markets for, U.S. agricultural products.

(f) * Promote multilateral trade, and agricultural and other economic development, under procedures established by the President, by loans or by use in any other manner determined by the President to be in the national interest of the United States, particularly to assist in the food programs in food-deficit countries friendly to the United States.

(g) Purchase goods or services for other friendly countries.

(h) * Finance programs on maternal welfare, child health and nutrition, and activities (where participation is voluntary) related to population growth problems.

(i) Pay the costs outside the United States for carrying out the program under section 406 of this act which authorizes assistance to friendly developing countries in becoming self-sufficient in food production.

(j) Sell for dollars those currencies determined to be in excess of the needs of U.S. departments and agencies to U.S. citizens and nonprofit organizations for travel or other purposes.

(k) * For paying, to the maximum extent practicable, the costs of carrying out programs for the control of rodents, insects, weeds, and other animal or plant pests.

*Denotes country-use programs (all other programs are U.S.-use).

☆ U. S. GOVERNMENT PRINTING OFFICE : 1970—434-916/ERS-17

UNITED STATES DEPARTMENT OF AGRICULTURE
WASHINGTON, D.C. 20250

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